

# **DIVIDER**

**STATE OF NORTH DAKOTA  
INFORMATION TECHNOLOGY DEPARTMENT  
SFN 2053 (4-2002)**

**PU-2304-00-270**

**Citizens Telecommunications Company of Minnesota,  
Local Exchange/IntraLATA Toll**

**Public Convenience & Nece**

**00**

**Filed 6/2/2000**

**Closed 2/8/2001**

**Scott, Sandi L.**

---

**From:** Bauske, Shelly A.  
**Sent:** Thursday, February 08, 2001 11:56 AM  
**To:** Geiger, Gloria A.; Scott, Sandi L.  
**Subject:** Money Received.....

Case No. PU-2304-00-269  
Case No. PU-2304-00-270  
Citizens Communications  
\$335.26

21 **PU-2304-00-270**

Pages: 0

\$335.26 received

by Citizens Telecommunications Company of Minneso

02/08/2001

CC: Comm Legal PUD (3)

**STATE OF NORTH DAKOTA**  
**PUBLIC SERVICE COMMISSION**

**Citizens Telecommunications Company of  
Minnesota, Inc.  
Local Exchange  
Public Convenience & Necessity**

**Case No. PU-2304-00-270**

**AFFIDAVIT OF SERVICE BY CERTIFIED MAIL**

STATE OF NORTH DAKOTA  
COUNTY OF BURLEIGH

**Sharon Helbling** deposes and says that:

she is over the age of 18 years and not a party to this action and, on the **8th day of February, 2001**, she deposited in the United States Mail, Bismarck, North Dakota, **one** envelope with certified postage, return receipt requested, fully prepaid, securely sealed and each containing a photocopy of:

**Order**

The envelope was addressed as follows:

Charles A Hoffman  
Maslon Edelman Borman & Brand  
3300 Norwest Ctr 90 S 7<sup>th</sup> St  
Minneapolis MN 55402-4140  
**Cert. No. 7000 0520 0022 8654 0421**

**Sharon Helbling** further deposes and says that on the **8th day of February, 2001**, she deposited in the United States Mail, Bismarck, North Dakota, **three** envelopes by regular mail, with postage fully prepaid, securely sealed, each containing a photocopy of the same.

Aloa Stevens  
Government Affairs-West  
Citizens Communications  
5600 Headquarters Dr  
Plano TX 75024


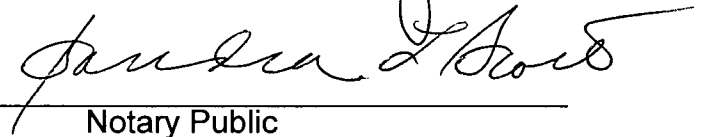
Lance Tade  
Citizens Communications  
9672 S 700 E Ste 101  
Sandy UT 84070-3555

Craig A Marks  
Citizens Utilities Company  
2901 N Central Ave Ste 1660  
Phoenix AZ 85012

Each address shown is the respective addressee's last reasonably ascertainable post office address.

Subscribed and sworn to before me  
this **8th day of February, 2001**.

SEAL

  
\_\_\_\_\_  
  
\_\_\_\_\_  
Notary Public

**SANDRA L. SCOTT**  
Notary Public, STATE OF NORTH DAKOTA  
My Commission Expires JUNE 11, 2004

**APPROVED**

**MOTION**

DATE: 2-7-01  
KMF

**February 7, 2001**

**Citizens Telecommunications Company of  
Minnesota, Inc.  
Local Exchange/IntraLATA Toll  
Public Convenience & Necessity**

**Case No. PU-2304-00-270**

I move the Commission adopt the Order and issued Certificates of Public Convenience and Necessity to provide local exchange and intraLATA interexchange toll services in the Oslo, Minnesota exchange, Case No. PU-2304-00-270.

sdh

**STATE OF NORTH DAKOTA**  
**PUBLIC SERVICE COMMISSION**

**Citizens Telecommunications Company of  
Minnesota, Inc.  
Local Exchange/IntraLATA Toll  
Public Convenience & Necessity**

**Case No. PU-2304-00-270**

**ORDER**

**February 7, 2001**

On May 27, 1999, Citizens Utilities Company and GTE entered into an agreement whereby Citizens agreed to purchase all of GTE's exchanges in the State of Minnesota. Citizens, through its subsidiaries, currently operates as an incumbent local exchange carrier in fourteen states and provides local, intraLATA and long distance services to approximately on million access lines in other states.

On June 2, 2000, Citizens Telecommunications Company of Minnesota, Inc. (CTCMN) filed an application for a certificate of public convenience and necessity to provide facilities-based local exchange telecommunications services as well as facilities-based intraLATA toll service for North Dakota customers served out of the Oslo exchange in Minnesota. CTCMN is purchasing the Oslo exchange from GTE Service Corporation.

On June 20, 2000, the Commission issued a Notice of Opportunity for Hearing, which provided until July 24<sup>th</sup> for receiving comments or hearing requests. No comments or requests for hearing were received. The notice identified the following issues:

1. Fitness and ability of the applicant to provide service.
2. Adequacy of the proposed service.
3. The technical, financial and managerial ability of the applicant to provide service.

On August 15, 2000, CTCMN filed an affidavit of Scott Bohler, Manager of State Government Affairs in the State of Minnesota. Scott Bohler set forth facts establishing the fitness and ability of CTCMN to provide local exchange service and intraLATA interexchange service, the adequacy of the proposed services, and the technical, financial and managerial ability of CTCMN to provide the requested services.

On August 23, 2000, the Public Service Commission's Director of Accounting filed a memorandum indicating that CTCMN has the financial ability to provide telecommunications service.

On January 11, 2001, CTCMN informed the Commission that the sale of the GTE telephone properties in Minnesota to CTCMN was closed.

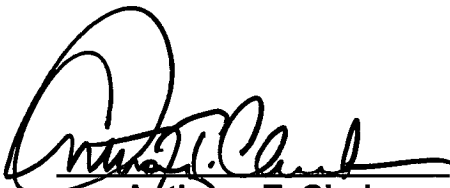
CTCMN is a wholly owned subsidiary of Citizens Communications Company, a diversified public utility that, through its various operating divisions or subsidiaries, operates as an incumbent local exchange carrier in fourteen states and provides local, intraLATA and long distance services to approximately one million access lines. The Commission finds CTCMN is fit, able, and has the technical, financial and managerial ability to provide telecommunications service.

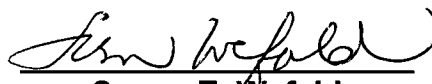
CTCMN intends to provide a full range of services to its customers. Services will include all local services, and may extend to include other advanced services. The Commission finds CTCMN's proposed service is adequate.

#### Order

1. The Commission orders the application of Citizens Telecommunications Company of Minnesota, Inc. for a certificate of public convenience and necessity to provide facilities-based local exchange telecommunications services to North Dakota customers served from the Oslo, Minnesota exchange is GRANTED.
2. The Commission orders the application of Citizens Telecommunications Company of Minnesota, Inc. for a certificate of public convenience and necessity to provide facilities-based intraLATA interexchange toll service in North Dakota for customers served from the Oslo, Minnesota exchange is GRANTED.
3. Citizens Telecommunications Company of Minnesota, Inc.'s certificates of public convenience and necessity shall be conditioned on securing such approval from local governing entities as required by state and federal law prior to providing service in any local territory.

#### PUBLIC SERVICE COMMISSION

  
Anthony T. Clark  
Commissioner

  
Susan E. Wefald  
President

  
Leo M. Reinbold  
Commissioner

# STATE OF NORTH DAKOTA

## Certificate of Public Convenience and Necessity

### Certificate Number 4673

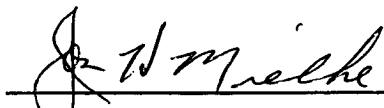
*This is to certify that public convenience and necessity require, and permission is granted for Citizens Telecommunications Company of Minnesota, Inc., a telecommunications public utility, to provide facilities-based local exchange telecommunications services to North Dakota customers served from the Oslo, Minnesota exchange.*

*This certificate is issued in Case No. PU-2304-00-270 and is conditioned upon Citizens Telecommunications Company of Minnesota, Inc. securing the franchise or other authority of the proper municipal or other authority for the exercise of these rights and privileges.*

*Bismarck, North Dakota, February 7, 2001.*

**ATTEST:**

**PUBLIC SERVICE COMMISSION**

  
Executive Secretary

  
Commissioner

# STATE OF NORTH DAKOTA

## Certificate of Public Convenience and Necessity

### Certificate Number 4674

*This is to certify that public convenience and necessity require, and permission is granted for Citizens Telecommunications Company of Minnesota, Inc., a telecommunications public utility, to provide facilities-based intraLATA interexchange (toll) service in North Dakota for customers served from the Oslo, Minnesota exchange.*

*This certificate is issued in Case No. PU-2304-00-270 and is conditioned upon Citizens Telecommunications Company of Minnesota, Inc. securing the franchise or other authority of the proper municipal or other authority for the exercise of these rights and privileges.*

*Bismarck, North Dakota, February 7, 2001.*

**ATTEST:**

**PUBLIC SERVICE COMMISSION**

  
Executive Secretary

  
Commissioner

**MASLON  
EDELMAN  
BORMAN  
& BRAND**

*Limited  
Liability Partnership*

MARVIN BORMAN  
NEIL I. SELL  
WILLIAM E. MULLIN  
WILLIAM Z. PENTELOVITCH  
JOSEPH ALEXANDER  
GARY J. HAUGEN  
THOMAS H. BORMAN  
MARK BAUMANN  
DAVID F. HERR  
R. LAWRENCE PURDY  
JAMES D. O'CONNOR  
RICHARD G. WILSON  
HOWARD B. TARKOW  
WILLIAM M. MOWER, P.A.  
LARRY A. KOCH, P.A.  
VIRGINIA A. BELL  
JUSTIN H. PERL  
COOPER S. ASHLEY  
SALLY STOLEN GROSSMAN  
MARTIN R. ROSENBAUM  
TERRI KRIVOSHA  
MARY R. VASALY  
JOHN W. PROVO  
EDWIN CHANIN  
CLARK T. WHITMORE  
WAYNE S. MOSKOWITZ  
CHARLES A. HOFFMAN  
MARK W. LEE  
LORRIE L. SALZL  
ALAIN M. BAUDRY  
RICHARD A. KEMPF  
SUSAN E. OLIPHANT  
JONATHAN S. PARRITZ  
KIRK O. KOLBO  
BRIAN J. KLEIN  
JAMES F. KILLIAN  
JAMES F. HANNEMAN  
SHERYL G. MORRISON  
DOUGLAS T. HOLOD  
ANDREW N. JACOBSON  
CYNTHIA F. GILBERTSON  
PENNY R. HEABERLIN  
MICHAEL C. MCCARTHY  
PHILIP J. TILTON  
R. CHRISTOPHER SUR  
SHAWN R. MCINTEE  
MARGARET C. HOBDDAY  
HOWARD A. ROSTON  
MARGARET M. KILLIAN  
MARGARET D. LUPKES  
MELISSA M. WELDON  
LAURA E. WALVOORD  
CHRISTOPHER J. MELSHA  
ALAN M. GILBERT  
KAI H. RICHTER  
LISA C. NETZER  
SCOTT L. GOODROAD

OF COUNSEL  
MARTIN G. WEINSTEIN  
MICHAEL L. SNOW  
ROYCE N. SANNER  
SUSAN J. LINK

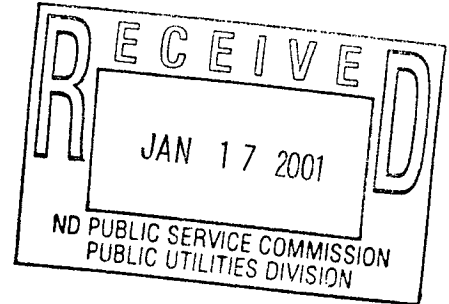
RETIRE  
CHARLES QUAINANCE, JR.  
ROBERT A. ENGELKE

SAMUEL H. MASLON  
1901-1988  
HYMAN EDELMAN  
1905-1993  
RUSSELL P. LEDERMAN  
1960-1999

3300 WELLS FARGO CENTER  
90 SOUTH SEVENTH STREET  
MINNEAPOLIS, MINNESOTA 55402-4140  
(612) 672-8200  
FAX (612) 672-8397  
www.maslon.com

Writer's Direct Dial  
672-8342

January 15, 2001



Patrick Fahn  
**NORTH DAKOTA PUBLIC  
SERVICE COMMISSION**  
State Capitol Building, 12<sup>th</sup> Floor  
Bismark, ND 58505

Re: **PU-2304-00-270**

Dear Pat:

I am following up on our telephone conversation of last week. I have forwarded to Mr. Mielke a copy of the FCC's Memorandum Opinion and Order granting the study area waiver relating to the ETC status of Citizens of North Dakota. A copy of that letter is being sent to you. With regards to the study area for Citizens Telecommunications of Minnesota, no application for a study area waiver was required. Citizens purchased the entirety of GTE's properties in the State of Minnesota and, as a result, there was no change in study area and no waiver was required. Hopefully this will clear up this matter and will permit the Commission to grant ETC status to Citizens Telecommunications of Minnesota, Inc.

Thank you very much for your consideration of this matter. As always, if you have any questions or comments, please do not hesitate to contact me.

Sincerely,

Charles A. Hoffman

CAH:sel:121550  
enclosure

cc Lance Tade

12 **PU-2304-00-269** Pages: 1  
Letter re FCC's Memo Opinion & Order  
by Citizens Telecommunications Company of Minneso  
01/17/2001 CC: Comm Legal PUD (3)

15 **PU-2304-00-270** Pages: 1  
Letter re FCC's Memo Opinion & Order  
by Citizens Telecommunications Company of Minneso  
01/17/2001 CC: Comm Legal PUD (3)

**MASLON  
EDELMAN  
BORMAN  
& BRAND**

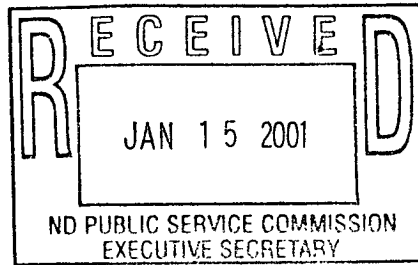
*Limited  
Liability Partnership*

MARVIN BORMAN  
NEIL I. SELL  
WILLIAM E. MULLIN  
WILLIAM Z. PENTELOVITCH  
JOSEPH ALEXANDER  
GARY J. HAUCEN  
THOMAS H. BORMAN  
MARK BAUMANN  
DAVID F. HERR  
R. LAWRENCE PURDY  
JAMES D. O'CONNOR  
RICHARD G. WILSON  
HOWARD B. TARKOW  
WILLIAM M. MOWER, P.A.  
LARRY A. KOCH, P.A.  
VIRGINIA A. BELL  
JUSTIN H. PERL  
COOPER S. ASHLEY  
SALLY STOLEN GROSSMAN  
MARTIN R. ROSENBAUM  
TERRI KRIVOSHA  
MARY R. VASALY  
JOHN W. PROVO  
EDWIN CHANIN  
CLARK T. WHITMORE  
WAYNE S. MOSKOWITZ  
CHARLES A. HOFFMAN  
MARK W. LEE  
LORRIE L. SALZL  
ALAIN M. BAUDRY  
RICHARD A. KEMPF  
SUSAN E. OLIPHANT  
JONATHAN S. PARRITZ  
KIRK O. KOLBO  
BRIAN J. KLEIN  
JAMES F. KILLIAN  
JAMES F. HANNEMAN  
SHERYL G. MORRISON  
DOUGLAS T. HOLOD  
ANDREW N. JACOBSON  
CYNTHIA F. GILBERTSON  
PENNY R. HEARBERLIN  
MICHAEL C. MCCARTHY  
PHILIP J. TILTON  
R. CHRISTOPHER SUR  
SHAWN R. McINTEE  
MARGARET C. HOBDDAY  
HOWARD A. ROSTON  
MARGARET M. KILLIAN  
MARGARET D. LUPKES  
MELISSA M. WELDON  
LAURA E. WALVOORD  
CHRISTOPHER J. MELSHA  
ALAN M. GILBERT  
KAI H. RICHTER  
LISA C. NETZER  
SCOTT L. GOODROAD

OF COUNSEL  
MARTIN G. WEINSTEIN  
MICHAEL L. SNOW  
ROYCE N. SANNER  
SUSAN J. LINK

RETIRED  
CHARLES QUAINANCE, JR.  
ROBERT A. ENGELKE

\* SAMUEL H. MASLON  
1901-1988  
HYMAN EDELMAN  
1905-1993  
RUSSELL F. LEDERMAN  
1960-1999



3300 WELLS FARGO CENTER  
90 SOUTH SEVENTH STREET  
MINNEAPOLIS, MINNESOTA 55402-4140  
(612) 672-8200  
FAX (612) 672-8397  
www.maslon.com  
Writer's Direct Dial  
672-8368

January 11, 2001

John Mielke  
Secretary  
North Dakota Public Service Commission  
State Capitol Building, 12<sup>th</sup> Floor  
Bismark, ND 58505

**Re: PU-2304-00-270**

Dear Mr. Mielke:

I am writing to inform you that the sale of the GTE telephone properties in Minnesota to Citizens Telecommunications of Minnesota, Inc. was closed on August 31, 2000.

Thank you very much for your consideration of this matter. If you have any questions or comments, please do not hesitate to contact me.

Sincerely,

Charles A. Hoffman

CAH/sel:120867

cc Lance Tade  
Scott Bohler

**MASLON  
EDELMAN  
BORMAN  
& BRAND**

*Limited  
Liability Partnership*

MARVIN BORMAN  
NEIL I. SELL  
WILLIAM E. MULLIN  
WILLIAM Z. PENTELOVITCH  
JOSEPH ALEXANDER  
GARY J. HAUGEN  
THOMAS H. BORMAN  
MARK BAUMANN  
DAVID F. HERR  
R. LAWRENCE PURDY  
JAMES D. O'CONNOR  
RICHARD G. WILSON  
HOWARD B. TARKOW  
WILLIAM M. MOWER, P.A.  
LARRY A. KOCH, P.A.  
VIRGINIA A. BELL  
JUSTIN H. PERL  
COOPER S. ASHLEY  
SALLY STOLEN GROSSMAN  
MARTIN R. ROSENBAUM  
TERRI KRIVOSHA  
MARY R. VASALY  
JOHN W. PROVO  
EDWIN CHANIN  
CLARK T. WHITMORE  
WAYNE S. MOSKOWITZ  
CHARLES A. HOFFMAN  
MARK W. LEE  
LORRIE L. SALZL  
ALAIN M. BAUDRY  
RICHARD A. KEMPF  
SUSAN E. OLIPHANT  
JONATHAN S. PARRITZ  
KIRK O. KOLBO  
BRIAN J. KLEIN  
JAMES F. KILLIAN  
JAMES F. HANNEMAN  
SHERYL G. MORRISON  
DOUGLAS T. HOLOD  
ANDREW N. JACOBSON  
CYNTHIA F. GILBERTSON  
PENNY R. HEABERLIN  
MICHAEL C. MCCARTHY  
PHILIP J. TILTON  
R. CHRISTOPHER SUR  
SHAWN R. MCINTEE  
MARGARET C. HOBBDAY  
HOWARD A. ROSTON  
MARGARET M. KILLIAN  
MARGARET D. LUPKES  
MELISSA M. WELDON  
LAURA E. WALVOORD  
CHRISTOPHER J. MELSHA  
ALAN M. GILBERT  
KAI H. RICHTER  
LISA C. NETZER  
SCOTT L. GOODROAD

OF COUNSEL  
MARTIN G. WEINSTEIN  
MICHAEL L. SNOW  
ROYCE N. SANNER  
SUSAN J. LINK

RETIRED  
CHARLES QUAINANCE, JR.  
ROBERT A. ENGELKE

SAMUEL H. MASLON  
1901-1988  
HYMAN EDELMAN  
1905-1993  
RUSSELL F. LEDERMAN  
1960-1999

Patrick Fahn  
**NORTH DAKOTA PUBLIC  
SERVICE COMMISSION**  
State Capitol Building, 12<sup>th</sup> Floor  
Bismark, ND 58505

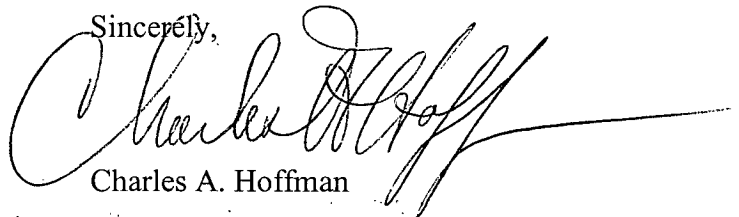
*Re: In the Matter of the Applications of Citizens Telecommunications  
Company of Minnesota, Inc.  
Case Nos.: PU-2304-00-269  
PU-2304-00-270*

Dear Mr. Fahn:

Sometime ago we discussed the information which you required in order to set the above two matters on for final approval by the North Dakota Commission. Specifically, you asked for the FCC study area number for the Citizens' territory in Minnesota which will provide service to the North Dakota exchange in question. We have now received that number. It is: 367123.

I hope that this information will be sufficient to finalize this matter. If there is other information you need or if you have any questions or comments, please do not hesitate to contact me.

Sincerely,



Charles A. Hoffman

CAH:sel:112708

11 PU-2304-00-269

Pages: 1

Letter re FCC study area number

by Citizens Telecommunications Company of Minneso

11/20/2000

CC: Comm Legal PUD (3)

13 PU-2304-00-270

Pages: 1

Letter re FCC study area number

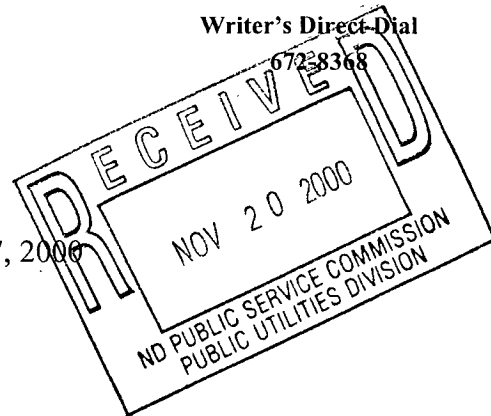
by Citizens Telecommunications Company of Minneso

11/20/2000

CC: Comm Legal PUD (3)

3300 WELLS FARGO CENTER  
90 SOUTH SEVENTH STREET  
MINNEAPOLIS, MINNESOTA 55402-4140  
(612) 672-8200  
FAX (612) 672-8397  
www.maslon.com

Writer's Direct-Dial



November 17, 2000

APPROVED:

DATE: 12-29-00

KME

MOTION

December 29, 2000

Citizens Telecommunications Company  
of Minnesota, Inc.  
Designated Eligible Carrier  
Application

Case No. PU-2304-00-269

Citizens Telecommunications Company  
of Minnesota, Inc.  
Local Exchange/IntraLATA Toll  
Public Convenience & Necessity

Case No. PU-2304-00-270

I move the Commission bill Citizens Telecommunications Company of  
Minnesota, Inc. for costs incurred to date in Case No. PU-2304-00-269, Citizens  
Telecommunications Company of Minnesota, Inc., Designated Eligible Carrier,  
Application and Case No. PU-2304-00-270, Citizens Telecommunications  
Company of Minnesota, Inc., Local Exchange/IntraLATA Toll, Public  
Convenience & Necessity.



**Public Service Commission**  
State of North Dakota

600 E Boulevard Ave. Dept. 408  
Bismarck, North Dakota 58505-0480  
e-mail: sab@oracle.psc.state.nd.us  
TDD 800-366-6888  
Fax 701-328-2410  
Phone 701-328-2400

COMMISSIONERS

Bruce Hagen  
President  
Susan E. Wefald  
Leo M. Reinbold

December 29, 2000

Executive Secretary  
Jon H. Mielke

Charles A Hoffman  
Maslon Edelman Borman & Brand  
3300 Norwest Center  
90 S 7th St  
Minneapolis MN 55402-4140

RE: Case No. PU-2304-00-269  
Citizens Telecommunications Company of Minnesota, Inc.  
Designated Eligible Carrier  
Application

Case No. PU-2304-00-270  
Citizens Telecommunications Company of Minnesota, Inc.  
Local Exchange/IntraLATA Toll  
Public Convenience & Necessity

Enclosed is a copy of the statement approved at the December 29, 2000  
Public Service Commission meeting for the expenses incurred to date in Case  
Nos. PU-2304-00-269 and PU-2304-00-270.

Under N.D.C.C. 49-21-01.7, these expenses are billed through the Valuation  
Fund and must be paid for by the telecommunications company involved.

Please make your check payable to the Public Service Commission.

Sincerely,

A handwritten signature in cursive script, appearing to read "Gloria Geiger".

Gloria Geiger  
Administrative Assistant  
701-328-2401

Enc.

c: Aloa Stevens  
Citizens Communications  
5600 Headquarters Dr  
Plano TX 75024  
  
Craig A Marks  
Citizens Utilities Company  
2901 N Central Ave Ste 1660  
Phoenix AZ 85012

Lance Tade  
Citizens Communications  
9672 South  
700 E Ste 101  
Sandy UT 84070-3555

## Billing Statement

December 29, 2000

Citizens Telecommunications Company  
of Minnesota, Inc.  
Designated Eligible Carrier  
Application

Case No. PU-2304-00-269

Citizens Telecommunications Company  
of Minnesota, Inc.  
Local Exchange/IntraLATA Toll  
Public Convenience & Necessity

Case No. PU-2304-00-270

### Expenses Incurred to Date:

Advertising Costs	\$335.26
-------------------	----------

### Amount Due:

Citizens Telecommunications Company of Minnesota, Inc.	\$335.26
---	----------

### Send Payment To:

Public Service Commission  
600 E Boulevard Ave Dept 408  
Bismarck ND 58505-0480

**Federal Tax ID 45-0309764**

STATE OF NORTH DAKOTA  
PUBLIC SERVICE COMMISSION

Citizens Telecommunications Company of  
Minnesota, Inc.  
Local Exchange  
Public Convenience & Necessity

Case No. PU-2304-00-270

**AFFIDAVIT OF SERVICE BY CERTIFIED MAIL**

STATE OF NORTH DAKOTA  
COUNTY OF BURLEIGH

**Sharon Helbling** deposes and says that:

she is over the age of 18 years and not a party to this action and, on the **23rd day of August, 2000**, she deposited in the United States Mail, Bismarck, North Dakota, **one** envelope with certified postage, return receipt requested, fully prepaid, securely sealed and each containing a photocopy of:

**Staff Memorandum on Financial Ability**

The envelope was addressed as follows:

Charles A Hoffman  
Maslon Edelman Borman & Brand  
3300 Norwest Ctr 90 S 7<sup>th</sup> St  
Minneapolis MN 55402-4140  
**Cert. No. 7099 3220 0002 8476 9033**

**Sharon Helbling** further deposes and says that on the **23rd day of August, 2000**, she deposited in the United States Mail, Bismarck, North Dakota, **three** envelopes by regular mail, with postage fully prepaid, securely sealed, each containing a photocopy of the same.

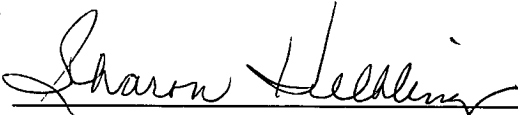
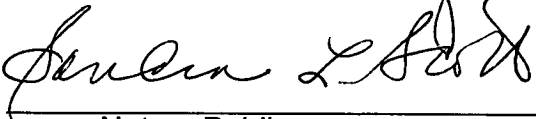
Aloa Stevens  
Government Affairs-West  
Citizens Communications  
5600 Headquarters Dr  
Plano TX 75024

Lance Tade  
Citizens Communications  
9672 S 700 E Ste 101  
Sandy UT 84070-3555

Craig A Marks  
Citizens Utilities Company  
2901 N Central Ave Ste 1660  
Phoenix AZ 85012

Each address shown is the respective addressee's last reasonably ascertainable post office address.

Subscribed and sworn to before me  
this **23rd day of August, 2000.**

  
\_\_\_\_\_  
  
\_\_\_\_\_

Notary Public

SEAL



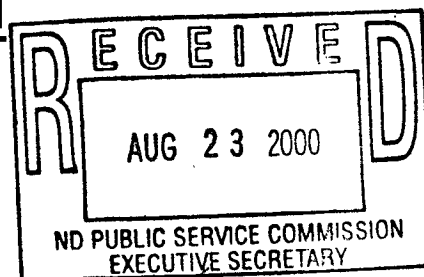
# Memorandum

To: Jon Mielke

From: Mike Diller *Mike Diller*

Date: August 23, 2000

Re: **Citizens Telecommunications Company of Minnesota  
Local Exchange / IntraLATA Toll PC&N Application  
PU-2304-00-270**



The following is written to provide the commission with a very limited review of this case regarding the Applicant's financial ability to serve.

According to the application, Citizens Telecommunication Company of Minnesota (Citizens Minnesota) has agreed to purchase all of GTE's exchanges in Minnesota and some of those exchanges provide service to customers in North Dakota. Citizens Minnesota is a wholly owned subsidiary of Citizens, a diversified public utility which provides telecommunications, electric, gas, water and wastewater services to approximately 1.9 million customers.

Citizen's is a publicly held corporation traded on the New York Stock Exchange under the symbol CZN. Staff reviewed the financial statements included in its application and agrees that Citizens Telco as a subsidiary of Citizens has the financial wherewithal to provide telecommunications service in North Dakota.

Staff sees no reason to deny Citizens Telco's application.

In accordance with the Commission's wishes, staff will serve this document on the applicant.

# INFORMAL AGENDA

August 16, 2000

- PU-2031-00-253      Bear Paw Energy, LLC  
Transfer Cert. Nos. 53, 63, Permit Nos. 60, 73  
Application
- PU-2304-00-269      Citizens Telecommunications Company of Minnesota, Inc.  
Designated Eligible Carrier  
Application
- PU-2304-00-270      Citizens Telecommunications Company of Minnesota, Inc.  
Local Exchange/IntraLATA Toll  
Public Convenience and Necessity

**10 PU-2031-00-253**

Pages: 1

Informal Hearing held

by Public Service Commission

08/16/2000

CC: Comm Legal PUD (3)

**9 PU-2304-00-269**

Pages: 1

Informal Hearing held

by Public Service Commission

08/16/2000

CC: Comm Legal PUD (3)

✓ **9 PU-2304-00-270**

Pages: 1

Informal Hearing held

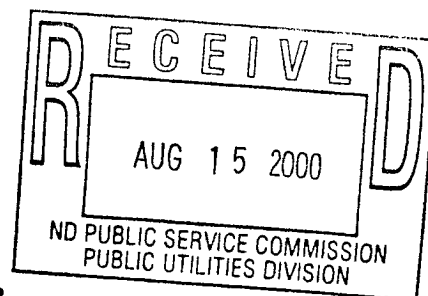
by Public Service Commission

08/16/2000

CC: Comm Legal PUD (3)

**BEFORE THE  
NORTH DAKOTA PUBLIC SERVICE COMMISSION**

In the Matter of the Application of )  
)  
CITIZENS TELECOMMUNICATIONS ) Case No. PU-2304-00-270  
COMPANY OF MINNESOTA )  
)  
For Authority to Operate as an )  
Incumbent Local Exchange )  
Provider in North Dakota )



**AFFIDAVIT OF SCOTT BOHLER**

STATE OF MINNESOTA )  
) ss.  
COUNTY OF HENNEPIN )

SCOTT BOHLER, being first duly sworn upon oath, deposes and says:

1. I am employed by Citizens Communications Company ("Citizens"). My title is Manager, State Government Affairs and my address is 2378 Wilshire Boulevard, Mound, Minnesota 55364.

2. In my role as Manager, State Government Affairs, I am responsible for management and implementation of regulatory and government affairs issues for Citizens local exchange telecommunications operations in the State of Minnesota. Among my responsibilities are implementation and oversight of regulatory policies and activities, including application for certificates of public convenience and necessity, interconnection agreements and state regulatory and legislative proceedings and relations.

3. I am making this Affidavit in support of the application of Citizens Telecommunications Company of Minnesota ("Citizens Minnesota") for authority to provide

**8 PU-2304-00-270**

Pages: 4

Affidavit of Scott Bohler

by Citizens Telecommunications Company of Minnesota  
08/15/2000 CC: Comm Legal PUD (3)

local exchange services in those Minnesota exchanges which have a limited number of customers in the state of North Dakota. I have personal knowledge of all facts stated herein. It is the purpose of this Affidavit to set forth facts establishing the adequacy of the proposed service, the technical, financial and managerial ability of Citizens Minnesota, and generally the fitness and ability of Citizens Minnesota to provide service.

4. On May 27, 1999, Citizens Utilities Company (now Citizens Communications Company) ("Citizens") and GTE entered into an agreement whereby Citizens agreed to purchase all of GTE's exchanges in the State of Minnesota (the "Agreement"). The entity providing service in Minnesota will be Citizens Telecommunications of Minnesota, Inc. ("Citizens Minnesota"). One of the GTE exchanges in Minnesota (Oslo) provides service to certain customers in North Dakota.

5. Citizens Minnesota is a wholly owned subsidiary of Citizens, a diversified public utility that, through its various operating divisions or subsidiaries, currently provides telecommunications, electric, gas, water and wastewater services to approximately 1.9 million customers in 22 states. Through subsidiaries, Citizens currently operates as an incumbent local exchange carrier ("ILEC") in fourteen states and provides local, intra-Lata and long-distance services to approximately one million access lines.

6. Citizens' business strategy is to focus on and expand the Communications Sector's operations. As part of that strategy, Citizens and GTE (or its affiliates) entered into a series of agreements on May 27, 1999, under which Citizens will purchase all of GTE's properties in Minnesota (approximately 117 exchanges, serving approximately 130,000 customers), and additional properties in Arizona and California.

7. Citizens and its subsidiary, Citizens Minnesota, clearly meet all technical, managerial, financial and legal qualifications required of applicants for a Certificate of Convenience and Necessity. Citizens Minnesota will draw heavily on the management resources of Citizens Communications for planning, marketing, network, service development, provisioning and delivery and legal/regulatory assistance. The above description of Citizens and its operations in 14 states establishes that it has broad experience in providing telecommunications services across the United States. That experience will enable Citizens to provide high quality service to its new customers in Minnesota.

8. In addition, all of the current employees of GTE Minnesota will remain as employees with Citizens Minnesota. This will provide continuity and an adequate work force to insure that the technical and managerial aspects of the business are continued with high quality.

9. Citizens intends to provide a full range of services to its Minnesota communications customers. Services will include all local services, and may expand to include other advanced services. Citizens currently contracts with AT&T to provide the nationwide-network for its long-distance products, which include fax/data communications, 800/888 service, international calling, calling cards and direct dial.

10. Citizens provides benefits to its employees consistent with those provided by leading U.S. companies, and supports its local communities. Citizens recognizes that GTE is a valued corporate citizen in the communities it serves and intends to continue that tradition.

11. Based on all of the above, Citizens respectfully asserts that it has demonstrated its fitness and ability to provide service, the adequacy of the service it proposes to provide, and that

Citizens has the technical, financial and managerial ability to provide the local exchange services for which certification is requested.

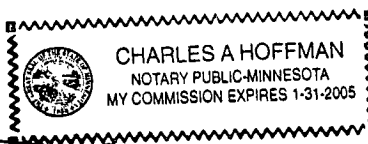
FURTHER AFFIANT SAYETH NOT.

*Scott Bohler*

\_\_\_\_\_  
Scott Bohler

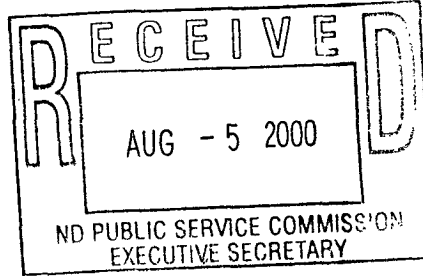
Subscribed and sworn to before me this  
15<sup>th</sup> day of August, 2000.

*Charles A Hoffman*  
\_\_\_\_\_  
Notary Public



# Affidavit of Publication

State of North Dakota )  
County of Burleigh )



Laurie Thiel, being duly sworn, state as follows:

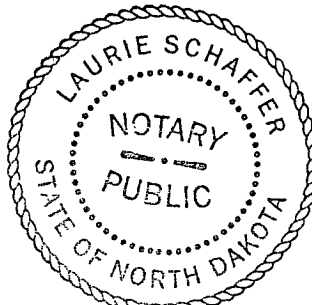
1. I am the designated agent, under the provisions and for the purposes of, Section 31-04-06, NDCC, for the newspapers listed on the attached exhibits.
2. The newspapers listed on the exhibits published the advertisement of:  
Citizens Telecomm., 1 time(s)  
as required by law or ordinance.
3. All of the listed newspapers are legal newspapers in the State of North Dakota and, under the provisions of Section 46-05-01, NDCC, are qualified to publish any public notice or any matter required by law or ordinance to be printed or published in a newspaper in North Dakota.

Signed: Laurie Thiel

Subscribed and sworn to before me this 18<sup>th</sup> day of July A.D. 2000

Laurie Schaffer

LAURIE SCHAFFER  
Notary Public, STATE OF NORTH DAKOTA  
My Commission Expires DEC. 1, 2005



7 PU-2304-00-269 Pages: 11  
08/04/2000  
North Dakota Advertising Service, Inc.  
Affidavit of Publication

CC: Comm Legal PUD (3)

7 PU-2304-00-270 Pages: 11  
08/04/2000  
North Dakota Advertising Service, Inc.  
Affidavit of Publication

CC: Comm Legal PUD (3)

Notice of Opportunity for Hearing  
June 20, 2000

Case # PU - 2304-00-270

Bismarck	6-20
Devils Lake	6-28
Dickinson	6-28
Fargo	7-3
Grand Forks	6-28
Jamestown	6-28
Minot	6-28
Valley City	6-28
Wahpeton	6-28
Williston	

STATE OF NORTH DAKOTA  
PUBLIC SERVICE COMMISSION

Citizens Telecommunications Company of  
Minnesota, Inc.  
Designated Eligible Carrier  
Application

Case No. PU-2304-00-269

Citizens Telecommunications Company of  
Minnesota, Inc.  
Local Exchange/IntraLATA Toll  
Public Convenience & Necessity

Case No. PU-2304-00-270

**AFFIDAVIT OF SERVICE BY CERTIFIED MAIL**

STATE OF NORTH DAKOTA  
COUNTY OF BURLEIGH

**Sharon Helbling** deposes and says that:

she is over the age of 18 years and not a party to this action and, on the **21st day of June, 2000**, she deposited in the United States Mail, Bismarck, North Dakota, **one** envelope with certified postage, return receipt requested, fully prepaid, securely sealed and each containing a photocopy of:

**Notice of Opportunity for Hearing**

The envelope was addressed as follows:

Charles A Hoffman  
Maslon Edelman Borman & Brand  
3300 Norwest Ctr 90 S 7<sup>th</sup> St  
Minneapolis MN 55402-4140  
**Cert. No. 7099 3220 0002 8476 7770**

**Sharon Helbling** further deposes and says that on the **21st day of June, 2000**, she deposited in the United States Mail, Bismarck, North Dakota, **three** envelopes by regular mail, with postage fully prepaid, securely sealed, each containing a photocopy of the same.

Aloa Stevens  
Government Affairs-West  
Citizens Communications  
5600 Headquarters Dr  
Plano TX 75024

Lance Tade  
Citizens Communications  
9672 S 700 E Ste 101  
Sandy UT 84070-3555

6 **PU-2304-00-270** Pages: 2  
06/21/2000  
Public Service Commission  
Affidavit of Service by Certified Mail

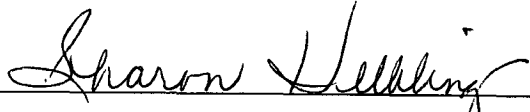
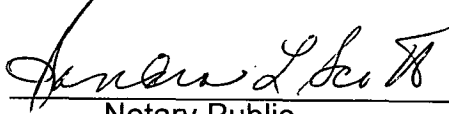
CC: Comm Legal PUD (3)

Craig A Marks  
Citizens Utilities Company  
2901 N Central Ave Ste 1660  
Phoenix AZ 85012

Each address shown is the respective addressee's last reasonably ascertainable post office address.

Subscribed and sworn to before me  
this **21st day of June, 2000.**

SEAL

  
\_\_\_\_\_  
  
\_\_\_\_\_  
Notary Public

**SANDRA L. SCOTT**  
Notary Public, STATE OF NORTH DAKOTA  
My Commission Expires **JUNE 11, 2004**

**STATE OF NORTH DAKOTA**  
**PUBLIC SERVICE COMMISSION**

**Citizens Telecommunications Company of  
Minnesota, Inc.  
Designated Eligible Carrier  
Application**

**Case No. PU-2304-00-269**

**Citizens Telecommunications Company of  
Minnesota, Inc.  
Local Exchange  
Public Convenience & Necessity**

**Case No. PU-2304-00-270**

**AFFIDAVIT OF SERVICE BY ORDINARY MAIL OR E-MAIL**

STATE OF NORTH DAKOTA  
COUNTY OF BURLEIGH

**Sharon Helbling** deposes and says that:

she is over the age of 18 years and not a party to this action and, on the **21st day of June, 2000**, she deposited in the United States Mail, Bismarck, North Dakota, envelopes by first class mail, fully prepaid, securely sealed, each containing a photocopy of:

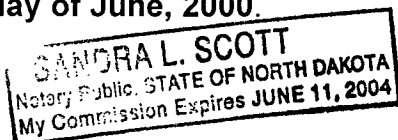
**Notice of Opportunity for Hearing**

The envelopes were addressed as follows:

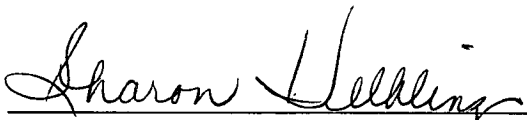
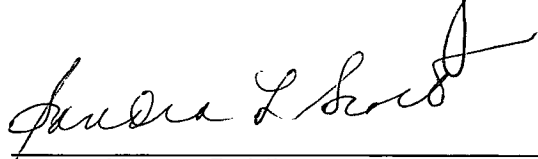
***See Attached List***

Each address shown is the respective addressee's last reasonably ascertainable post office address.

Subscribed and sworn to before me  
this **21st day of June, 2000**.



SEAL

  
\_\_\_\_\_  
  
\_\_\_\_\_  
Notary Public

**5 PU-2304-00-270**

Pages: 13

06/21/2000

Public Service Commission

Affidavit of Service by Ordinary Mail or E-Mail

CC: Comm Legal PUD (3)

**PU-2304-00-270**

Copies To:

State Library (8 copies)

Historical Society

Associated Press

donlee@martin-associates.com  
Don Lee  
81 Grand St  
New York NY 10013

j1chapman@acomminc.com  
Jerry Chapman  
Acomm Inc  
510 1st Ave N Ste 203  
Minneapolis MN 55403-0343

jtmgr@bektel.com  
Jerome Tishmack  
BEK Communications Cooperative  
PO Box 230  
Steele ND 58482-0230

ken@staff.ctctel.com  
L Dan Wilhelmson  
Consolidated Comm Networks Inc  
PO Box 1077  
Dickinson ND 58601-1077

ken@staff.ctctel.com  
L Dan Wilhelmson  
Consolidated Telephone Cooperative  
PO Box 1077  
Dickinson ND 58601-1077

meredith.gifford@gecapital.com  
Meredith Gifford  
GE Capital Comm Services Corp  
6540 Powers Ferry Rd  
Atlanta GA 30339

r1aqua@rrv.net  
Ronald Laqua  
Halstad Telephone Company  
PO Box 55  
Halstad MN 56548-0055

dc1ark@hq.idt.net  
Diane Clark  
IDT Corporation  
190 Main St  
Hackensack NJ 07601

nlarsen@nvc.com  
Clint Hansel  
Accent Communications Inc  
235 E 1st Ave  
Groton SD 57445

smassey@bepc.com  
Sheryl Massey  
Basin Electric Power Coop  
1717 E Interstate Ave  
Bismarck ND 58501-0564

jtmgr@bektel.com  
Jerome Tishmack  
BEK Communications I Inc  
PO Box 230  
Steele ND 58482-0230

ken@staff.ctctel.com  
L Dan Wilhelmson  
Consolidated Telcom Inc  
PO Box 1077  
Dickinson ND 58601-1077

drtc@drtel.net  
Roger L Johnson  
Dickey Rural Telephone Cooperative  
PO Box 69  
Ellendale ND 58436-0069

cooperstown@m1gc.com  
Ray Brown  
Griggs County Telephone Company  
Cooperstown ND 58425

hold@texas.net  
Dana Wilson  
Home Owners Long Distance Inc  
8647 wurzbach Rd #M-1  
San Antonio TX 78240-1245

kander@ictc.com  
Keith Anderson  
Inter-Community Telephone Co  
PO Box 8  
Nome ND 58062-0008

kander@ictc.com  
Keith Anderson  
Inter-Community Telephone Co. II  
PO Box 8  
Nome ND 58062-0008

itci@means.net  
Bruce Reube  
Interstate Telcom Consulting Inc  
130 Birch Ave W  
Hector MN 55342-0668

nschmid@acginc.net  
Neil Schmid  
Ionex Communications North Inc  
5710 LBJ Frwy Ste 215  
Dallas TX 75240

skat@means.net  
Steven Katka  
Loretel Systems Inc  
13 E 4th Ave  
Ada MN 56510

Michel.Murray@MCI.com  
Michel Murray  
MCI WorldCom Inc  
707 17th St Ste 3600  
Denver CO 80202

skillebrew@deltacom.com  
Sharon Killebrew  
McLeodUSA

john\_sullivan@cable.comcast.com  
John Sullivan  
McLeodUSA

whaas@mcleodusa.com  
William Haas  
McLeodUSA  
P O Box 3177  
Cedar Rapids IA 52406-3547

amy.ibis@dtg.com  
Amy Ibis  
McLeodUSA  
140 North Phillips Ave Ste 404  
Sioux Falls SD 57104-6711

gerrya@midrivers.com  
Gerry Anderson  
Mid-Rivers Telephone Coop Inc  
PO Box 280  
Circle MT 59215-0280

sbunn@mlgc.com  
Shelie Bunn  
Moore & Liberty Telephone Co  
Enderlin ND 58027

hfuglest@ndarec.com  
Harlan Fugelsten  
ND Assn Rural Electric Coops  
PO Box 727  
Mandan ND 58554-0727

dhill@ndarec.com  
Dennis Hill  
ND Assn Rural Electric Coops  
PO Box 727  
Mandan ND 58554-0727

pschaner@ndarec.com  
Patti Schaner  
ND Assn Rural Electric Coops  
PO Box 727  
Mandan ND 58554-0727

lclemens@nft.net  
Larry Clemens  
Noonan Farmers Tele Co  
Noonan ND 58765

rer@norlight.com  
Robert E Rogers  
NorLight Inc  
275 N Corporate Dr  
Brookfield WI 53045

cajuul@norstan.com  
Cathy Juul  
Norstan Network Services Inc  
P O Box 5715  
Minnetonka MN 5534333-57

klund@nccray.com  
Kenneth Lund  
Northwest Communications Corp  
PO Box 38  
Ray ND 58849-0038

jram@erols.com  
John Ramsey  
Parcel Consultants Inc  
150 Commerce Rd  
Cedar Grove NJ 07009

ddunning@polarcomm.com  
David Dunning  
Polar Telcom Inc  
PO Box 270  
Park River ND 58270-0270

jvonduyke@phoneforall.com  
Jeff Walker  
Preferred Carrier Services Inc  
14681 Midway Rd Ste 105  
Dallas TX 75244

pam@tnics.com  
Pamela Harrington  
RC Communications Inc  
PO Box 197  
New Effington SD 57255-0197

ardondoran@rrt.net  
Ardon Doran  
Red River Telecom Inc  
PO Box 136  
Abercrombie ND 58001-0136

mbrestel@ndak.net  
Marcia Burckhard  
Reservation Telephone Cooperative  
Parshall ND 58770

pagndta@btig- .com  
Patricia G. inger  
North Dakota Telephone Assoc  
PO Box 2614  
Bismarck ND 58502-2614

royce@restel.net  
Royce Aslakson  
Parcel Consultants Inc  
150 Commerce Rd  
Cedar Grove NJ 07009

ddunning@polarcomm.com  
David Dunning  
Polar Commun Mut Aid Corp  
PO Box 270  
Park River ND 58270-0270

ddunning@polarcomm.com  
David Dunning  
Polar Telecommunications Inc  
PO Box T  
Park River ND 58270

protel@citilink.com  
Scott Lee  
Protel Advantage Inc  
1144 Larpenteur Ave W  
St Paul MN 55113-6317

ardondoran@rrt.net  
Ardon Doran  
Red River Rural Tele Assoc  
PO Box 136  
Abercrombie ND 58001

jdbtbb@ndak.net  
Jan Boschee  
Reservation Telephone Cooperative  
Parshall ND 58770

pam@tnics.com  
Pamela Harrington  
Roberts Cty Tele Coop Assoc  
New Effington SD 57255

warrenlh@srttel.com  
Warren Hight  
Souris River Tele Coop  
PO Box 2027  
Minot ND 58702-2027

stevedl@srttel.com  
Steve Lysne  
SRT Communications Inc  
P O Box 789  
Minot ND 58702-0789

lynnan@srttel.com  
Lynn Nelson  
SRT Communications Inc  
P O Box 789  
Minot ND 58702-0789

davidrs@srttel.com  
David Smith  
SRT Communications Inc  
P O Box 789  
Minot ND 58702-0789

mdickers@state.nd.us  
Marcy Dickerson  
State Tax Department  
State Capitol  
Bismarck ND 58505

clarson@telegroup.com  
Caroline Larson  
Telegroup Inc  
2098 Nutmeg Ave  
Fairfield IA 52556

thomasc@totaltel.com  
Tom Carroll  
TotalTel Inc  
150 Clove Rd 8th Fl  
Little Falls NJ 07424

maryg@uslink.net  
Mary Goodman  
U S Link Inc  
200 2nd St  
Pequot Lakes MN 56472

suelh@srttel.com  
Sue Hamilton  
SRT Communications Inc  
P O Box 789  
Minot ND 58702-0789

christm@srttel.com  
Chris Morsefield  
SRT Communications Inc  
P O Box 789  
Minot ND 58702-0789

johnar@srttel.com  
John Reiser  
SRT Communications Inc  
P O Box 789  
Minot ND 58702-0789

kimrw@srttel.com  
Kim Weydahl  
SRT Communications Inc  
P O Box 789  
Minot ND 58702-0789

grndelec@iw.net  
Darrell Henderson  
Stateline Telecomm Inc  
PO Box 39  
Bison SD 57620-0039

bgreene@magicnet.net  
Barbara Greene  
Telephone Co of Central Florida Inc  
3599 W Lake Mary Blvd Ste E  
Lake Mary FL 32746-3417

bpipkin@touch1.com  
Leigh Ann Wooten  
Touch 1 Long Distance Inc  
100 Brookwood Rd  
Atmore AL 36502

tahall@usgs.gov  
Lenora Hall  
U S Geological Survey

kjvannin@usgs.gov  
K Vannin  
U S Geological Survey

afranklin@usouth.net  
Anne Franklin  
U S South Communications Inc  
250 Williams St Ste 2360  
Atlanta GA 30303

ralyana@uswest.com  
Richard Alyanak  
U S WEST

tkunkle@uswest.com  
Timothy Kunkleman  
U S WEST  
1801 California St Rm 4630  
Denver CO 80202

smacint@uswest.com  
Scott Macintosh  
U S WEST Communications Inc  
PO Box 5508  
Bismarck ND 58502-5508

jmunnn@uswest.com  
John Munn  
U S WEST Communications Inc  
1801 California Rm 5100  
Denver CO 80202

saberry@uswest.com  
Sharon Berry  
U S WEST Communications Inc  
409 1st Ave N  
Fargo ND 58102-4802

sschwan@uswest.com  
Suzy Schwandt  
U S WEST Communications, Inc.  
P O Box 5508  
Bismarck ND 58502-5508

johng@unidial.com  
John Greive  
UniDial Communications Inc  
1901 Eastpoint Pkwy  
Louisville KY 40223

kander@ictc.com  
Keith Anderson  
Valley Communications Inc  
P O Box 8  
Nome ND 58062

tsusak@vocall.com  
Tony Susak  
VoCall Communications Corp  
284 Sheffield St  
Mountainside NJ 07092

bonniek@westriv.com  
Bonnie Krause  
West River Telecomm Coop  
PO Box 467  
Hazen ND 58545-0467

pihland@means.net  
Paul Ihland  
Wolverton Telephone Company  
Wolverton MN 56594

Neil Talbot  
81 Grand St  
New York NY 10013

Myer Shark  
2277 Gene Autry Trail Unit C  
Palm Springs CA 92264

Myer Shark  
Knollwood Place Apts #221  
3630 Phillips Pkwy  
St Louis Park MN 55426

Ann Faught  
Absaraka Co-op Tele Co  
Absaraka ND 58002

ACN Communications Services Inc  
32991 Hamilton Ct  
Farmington Hills MI 48334

Mark Waind  
Altru Health System  
1200 South Columbia Rd  
Grand Forks ND 58201

John Summers  
AmeriTel Pay Phones Inc  
180 Northwest Oldham Pkwy  
Lee's Summit MO 64081

Arch Paging  
11437 Valley View Rd  
Eden Prairie MN 55344

Leeann Brunnette  
AT&T  
321 E Walnut St  
Des Moines IA 50309

Jack Medaris  
Atlas Communications LTD  
484 Norristown Rd Ste 123  
Blue Bell PA 19422

Dorothy Jones  
Bell Atlantic Communications Inc  
1320 N Courthouse Rd 9th Fl  
Arlington VA 22201

Jennifer Whitley  
Business Discount Plan Inc  
3780 Kilroy Arpt Wy  
Long Beach CA 90806

John Session  
Cable & Wireless Comm Inc  
8219 Leesburg Pike  
Vienna VA 22182

Scott Geston  
Cable One of Fargo  
P O Box 10624  
Fargo ND 58106-0624

Choctaw Communications Inc  
1600 Viceroy  
Dallas TX 75235

Robert Fallan  
Coast International  
14303 W 95th St  
Lenexa KS 66215-5210

Comcast Telecommunications  
1500 Market St  
Philadelphia PA 19102

Molli Harper  
Commnet Cellular Inc  
8350 E Crescent Pkwy Ste 400  
Englewood CO 80111

Murray Barr  
Competitive Strategies Group Inc  
70 East Lake St 7th Fl  
Chicago IL 80112

Elaine McHale  
Concert Communications Sales LLC  
295 N Maple Ave Rm 5463A2  
Basking Ridge NJ 07920

D D D Calling Inc  
5120 Woodway Ste 8020  
Houston TX 77056

Robert Hill  
Dakota Central Telecom I  
PO Box 299  
Carrington ND 58421-0299

Dickey Rural Communications Inc  
PO Box 69  
Ellendale ND 58436-0069

Easton Telecom Services Inc  
4646 W Streetsboro  
Richfield OH 44286

Lawrence Freedman  
Fleischman & Walsh  
1400 16th ST NW  
Washington DC 20036

Ronald Rodemerk  
Frontier Comm International  
180 S Clinton Ave  
Rochester NY 14646-0500

Lucille Nilson  
Griggs County Telephone Company  
Cooperstown ND 58425

HJN Telecom Inc  
3235 Satellite Blvd Bldg 400 Ste 300  
Duluth GA 30096

Lance Sentman  
International Telcom Ltd  
417 2nd Ave W  
Seattle WA 98119

Nanette Edwards  
ITC DELTACOM INC  
4092 Memorial Pkwy SW  
Huntsville AL 35802-1382

Robert Hill  
Dakota Central Tele Coop  
PO Box 299  
Carrington ND 58421-0299

Darcy Delaney  
DavelTel Inc  
10120 Windhorst Rd  
Tampa FL 33619

DSLnet Communications LLC  
545 Long Wharf Dr  
New Haven CT 06511

Excel Communications Inc  
P O Box 650582  
Dallas TX 75265

Framco Inc  
P O Box 2711  
Fargo ND 58108

Craig Brewerton  
Geo Economics  
PO Box 4272  
Missoula MT 59806-4272

Group Long Distance Inc  
6600 N Andrews Ave Ste 140  
Ft Lauderdale FL 33309

IdeaOne Telecom Group LLC  
3239 39th St SW  
Fargo ND 58104

Sue Weiske  
Ionex Communications North Inc  
5710 LBJ Frwy Ste 215  
Dallas TX 75240

Larry Barnes  
IXC/SSC-Regulatory Affairs  
1122 S Capital of TX Hwy  
Austin TX 78746-6426

Thomas K Crowe  
Law Offices of Thomas K Crowe PC  
2300 M St NW Ste 800  
Washington DC 20037

LCI International Telecom Corp  
4650 Lakehurst Ct  
Dublin OH 43017

LDM Systems Inc  
430 Park Ave 5th Fl  
New York NY 10022

Level 3 Communications LLC  
3555 Farnam St  
Omaha NE 68131

Jan Lowe  
Long Dist Consolidated Billing Co  
145 S Livernois Rd #199  
Rochester MI 48307-1837

Marilyn Foss  
MCI WorldCom Inc  
707 17th St Ste 3600  
Denver CO 80202

MCImetro Access Transmission Services  
1801 Pennsylvania Ave NW  
Washington DC 20006

McLeodUSA  
P O Box 3177  
Cedar Rapids IA 52406-3177

Carolyn Fodor  
MIDCOM Communications Inc  
26913 Northwestern Hwy #165  
Southfield MI 48034

Midcontinent Communications  
410 South Phillips Ave  
Sioux Falls SD 57104

Mid-Rivers Telephone Coop Inc  
P O Box 280  
Circle MT 59215

Gordon Wilhelmi  
Midstate Communications Inc  
PO Box 400  
Stanley ND 58784-0400

Mark Wilhelmi  
Midstate Telephone Co  
PO Box 400  
Stanley ND 58784-0400

Minnesota Independent Equal Access  
Corp  
10300 6th Avenue N  
Plymouth MN 55441

Mike Strand  
MITS  
PO Box 5237  
Helena MT 59604-5237

MVX Communications LLC  
100 Rowland Way Ste 145  
Novato CA 94945

Dave Crothers  
NDATC  
Box 1144  
Mandan ND 58554-1144

Richard Thronson  
Nemont Telephone Cooperative Inc  
Scobey MT 59263

Sharon Meinhart  
NetLogix Telecom Inc  
501 Bath St  
Santa Barbara CA 93101

Net-tel Corporation  
1023 31st St NW  
Washington DC 20007

Nextel West Corp  
2001 Edmund Halley Dr  
Reston VA 20191-3436

Holly Sasscer  
Operator Communications Inc  
3530 Forest Ln Ste 200  
Dallas TX 75234-7910

Pamcomm  
P O Box 5200  
Sioux Falls SD 57117-5200

Primus Telecommunications Inc  
1700 Old Meadow Rd 3rd Fl  
McLean VA 22102

Quintelco Inc  
1 Blue Hill Plaza  
Pearl River NY 10965

Dean Polkow  
RCC Network Inc  
PO Box 2000  
Alexandria MN 56308-2000

Gene Sloan  
Reservation Telephone Cooperative  
Parshall ND 58770

Lisa Dabkowski  
SNET America Inc  
6 Devine St 1st Fl  
North Haven CT 06743

Randy Burckhard  
SRT Communications Inc  
P O Box 789  
Minot ND 58702-0789

Target Telecom Inc  
1515 S Federal Hwy Ste 400  
Boca Raton FL 33432-7451

Dave Dirck  
North Dakota Telephone Company  
PO Box 180  
Devils Lake ND 58301-0180

Patrick Delaney  
Overlook Communications International  
3125 North Meadow Pkwy #S110  
Roswell GA 30076

Bryan Engle  
Parcel Consultants Inc  
150 Commerce Rd  
Cedar Grove NJ 07009

Jan Sebby  
Pringle and Herigstad P C  
PO Box 1000  
Minot ND 58702-1000

Heather Troxell  
Qwest Communications Corporation  
4250 Fairfax Dr  
Arlington VA 22203

RCN Long Distance Company  
105 Carnegie Ctr  
Princeton NJ 08540

Skyland Technologies Inc  
P O Box 5237  
Helena MT 59604-5237

Andrew Jones  
Sprint  
8140 Ward Pkwy Flr 5E  
Kansas City MO 64114

Harris Saele  
T P C Inc  
PO Box 180  
Devils Lake ND 58301-0180

Regulatory Analyst  
Technologies Management Inc  
PO Drawer 200  
Winter Park FL 32790-0200

Thomas Cirrito  
Telco Communications  
1100 Wilson Blvd Ste 1425  
Arlington VA 22209-2297

Jack Medar  
Telco Partners Inc  
484 Norristown Rd Ste 123  
Blue Bell PA 19422

Al Bosch  
Tele-Beep Company  
PO Box 7072  
Bismarck ND 58502-7072

Tele-Tech Inc  
2900 W 11th St  
Sioux Falls SD 57104-3660

Liz Petroni  
Teltrust Comm Services Inc  
6322 S 3000 East  
Salt Lake City UT 84121

T-Netix Inc  
67 Inverness Drive E  
Englewood CO 80112

Kenneth Carlson  
Turtle Mountain Communications  
PO Box 729  
Langdon ND 58249-0729

Judy Pepler  
U S WEST Communications Inc  
PO Box 5508  
Bismarck ND 58502-5508

Tim Kunkelman  
U S WEST Communications Inc  
1801 California St Rm 4630  
Denver CO 80202

Dick Boyer  
U S West Interprise America Inc  
1999 Bdwy Rm 700  
Denver CO 80202

Giuseppe Vitale  
UKI Communications Inc  
500 N Rainbow Blvd Ste 300  
Las Vegas NV 89107

Sam Billingsley  
United States Advanced Network Inc  
3000 Northwoods Pkwy Ste 140  
Norcross GA 30071

Kenneth Carlson  
United Telephone Mut Aid Corp  
Langdon ND 58249

Dennis Houston  
Universal Network Services of ND  
1572 North Batavia St Ste 1A  
Orange CA 92867

Telecomm Dept  
University of North Dakota  
Box 8193  
Grand Forks ND 58202-7141

USBG Inc  
5601 W 120th St  
Alsip IL 60658

Val-Ed Joint Venture LLP  
150 2nd St SW  
Perham MN 56573

Randy Houdek  
Venture Communications Inc  
PO Box 157  
Highmore SD 57345-0157

Robert Barfield  
West River Communications Inc  
PO Box 467  
Hazen ND 58545-0467

Doris Cooper  
West River Long Distance Co  
PO Box 467  
Hazen ND 58545-0467

Robert Barfield  
West River Telecomm Coop  
PO Box 467  
Hazen ND 58545-0467

Western CLCC Corporation  
3650 131st Ave SE #400  
Bellevue WA 98006

Z-Tel Communications Inc  
601 S Harbour Island Blvd Ste 220  
Tampa FL 33602-5925

**Helbling, Sharon D.**

---

**From:** Helbling, Sharon D.  
**Sent:** Wednesday, June 21, 2000 8:39 AM  
**To:** 'ndna'  
**Subject:** Attached Notices

Please have the attached Notices published as legal publications in the next issue of the ten North Dakota daily newspapers. Would you also run them as "News Item Only" articles.

Send the bill to the Public Service Commission along with a tear sheet for billing purposes.

If you have any questions, please call me at 701-328-4076.

Thank you.

**Sharon Helbling**  
**Public Utilities Division**

1.doc

1.doc

4 **PU-2304-00-270**

Pages: 1

06/21/2000

Public Service Commission

Notice E-Mailed to NDNA requesting

publication

1

CC: Comm Legal PUD (3)

**MOTION**

**June 20, 2000**

**Citizens Telecommunications Company of  
Minnesota, Inc.  
Designated Eligible Carrier  
Application**

**Case No. PU-2304-00-269**

**Citizens Telecommunications Company of  
Minnesota, Inc.  
Local Exchange/IntraLATA Toll  
Public Convenience & Necessity**

**Case No. PU-2304-00-270**

I move the Commission issue a Notice of Opportunity for Hearing in the applications of Citizens Telecommunications Company of Minnesota, Inc. for Designated Eligible Carrier status, Case No. PU-1204-00-269 and for Certificates of Public Convenience and Necessity to provide telecommunications services in North Dakota, Case No. PU-2304-00-270.

JRL/sdh

000270-2.doc

**STATE OF NORTH DAKOTA**

**PUBLIC SERVICE COMMISSION**

**Citizens Telecommunications Company of  
Minnesota, Inc.  
Designated Eligible Carrier  
Application**

**Case No. PU-2304-00-269**

**Citizens Telecommunications Company of  
Minnesota, Inc.  
Local Exchange/IntraLATA Toll  
Public Convenience & Necessity**

**Case No. PU-2304-00-270**

**NOTICE OF OPPORTUNITY FOR HEARING**

**June 20, 2000**

On June 2, 2000, Citizens Telecommunications Company of Minnesota, Inc. (Citizens of MN) filed an application for a certificate of public convenience and necessity to provide facilities-based local exchange telecommunications services as well as facilities based intraLATA toll service for North Dakota customers served out of the Oslo exchange in Minnesota. Citizens of MN is purchasing the Oslo exchange from GTE Service Corporation. Citizens of MN also requests designation as an Eligible Telecommunications Carrier (ETC) for this area.

The issues to be considered in these matters are:

1. Fitness and ability of the applicant to provide service.
2. Adequacy of the proposed service.
3. The technical, financial and managerial ability of the applicant to provide service.
4. Qualification under the Telecommunications Act of 1996, Section 214(e) for designation as an ETC eligible to receive federal universal service funding.
5. Designated ETC universal service support area.

Those interested are invited to comment on these applications in writing. Persons desiring a hearing must file a written request identifying their interest in the proceeding and the reasons for requesting a hearing. Comments and requests for

hearings must be received by **July 24, 2000**. If deemed appropriate, the Commission can determine these matters without hearings.

For more information contact the Public Service Commission, State Capitol, Bismarck, North Dakota 58505, 701-328-2400; or Relay North Dakota 1-800-366-6888 TTY. If you require any auxiliary aids or services, such as readers, signers, or Braille materials please notify Jon Mielke, Executive Secretary.

**PUBLIC SERVICE COMMISSION**

  
\_\_\_\_\_  
**Susan E. Wefald**  
Commissioner

  
\_\_\_\_\_  
**Bruce Hagen**  
President

  
\_\_\_\_\_  
**Leo M. Reinbold**  
Commissioner

**MASLON  
EDELMAN  
BORMAN  
& BRAND**

*Limited  
Liability Partnership*

MARVIN BORMAN  
NEIL I. SELL  
WILLIAM E. MULLIN  
WILLIAM Z. PENTELOVITCH  
JOSEPH ALEXANDER  
GARY J. HAUGEN  
THOMAS H. BORMAN  
MARK BAUMANN  
DAVID F. HERR  
R. LAWRENCE PURDY  
JAMES D. O'CONNOR  
RICHARD G. WILSON  
HOWARD B. TARKOW  
WILLIAM M. MOWER, P.A.  
LARRY A. KOCH  
VIRGINIA A. BELL  
JUSTIN H. PERL  
COOPER S. ASHLEY  
SALLY STOLEN GROSSMAN  
MARTIN R. ROSENBAUM  
TERRI KRIVOSHA  
MARY R. VASALY  
JOHN W. PROVO  
EDWIN CHANIN  
CLARK T. WHITMORE  
WAYNE S. MOSKOWITZ  
CHARLES A. HOFFMAN  
MARK W. LEE  
LORRIE L. SALZL  
ALAIN M. BAUDRY  
RICHARD A. KEMPF  
SUSAN E. OLIPHANT  
JONATHAN S. PARRITZ  
KIRK O. KOLBO  
BRIAN J. KLEIN  
JAMES F. KILLIAN  
JAMES F. HANNEMAN  
SHERYL G. MORRISON  
DOUGLAS T. HOLOD  
NEIL P. AVOTTE  
ANDREW N. JACOBSON  
CYNTHIA F. GILBERTSON  
PENNY R. HEABERLIN  
LAURIE A. KINDEL  
MICHAEL C. McCARTHY  
PHILIP J. TILTON  
R. CHRISTOPHER SUR  
SHAWN R. McINTEE  
MARGARET C. HOBDA  
HOWARD A. ROSTON  
MARGARET M. KILLIAN  
PETER J. CARLTON  
STEPHEN A. TIGHT  
MARGARET D. LUPKES  
MELISSA M. WELDON  
LAURA E. WALVOORD  
CHRISTOPHER J. MELSHA  
ALAN M. GILBERT  
KAI H. RICHTER  
LISA C. NETZER

OF COUNSEL  
MARTIN G. WEINSTEIN  
MICHAEL L. SNOW  
ROYCE N. SANNER  
SUSAN J. LINK

RETIRED  
CHARLES QUAINANCE, JR.  
ROBERT A. ENGELKE

SAMUEL H. MASLON  
1901-1988  
HYMAN EDELMAN  
1905-1993

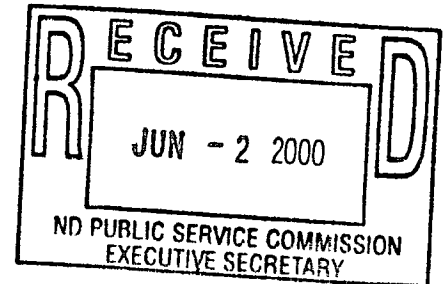
3300 NORWEST CENTER  
90 SOUTH SEVENTH STREET  
MINNEAPOLIS, MINNESOTA 55402-4140  
(612) 672-8200  
FAX (612) 672-8397

Writer's Direct Dial  
672-8368

May 25, 2000

**BY FEDERAL EXPRESS**

John Mielke  
Secretary  
North Dakota Public Service Commission  
State Capitol Building, 12<sup>th</sup> Floor  
Bismark, ND 58505



Re: Citizens Telecommunications Company of Minnesota  
Revised Application for a Certificate of Public Convenience and  
Necessity to Provide Local Telecommunication Services

Dear Mr. Mielke:

Enclosed for filing on behalf of Citizens Telecommunications Company of Minnesota ("Citizens Minnesota") are an original and eight copies of its Revised Application for a Certificate of Public Convenience and Necessity to Provide Local Telecommunication Services in the state of North Dakota. As this is a revised Application, I would request that you substitute this document for the existing Application on file with your office. I have not provided additional copies of the Exhibits filed with the original Application. However, I am providing appropriate copies of the additional Exhibits which are filed with this document. Please date stamp one copy and return it to the undersigned in the enclosed envelope provided.

If you have any questions concerning this filing, please do not hesitate to contact me.

Sincerely,

Charles A. Hoffman  
Counsel for Citizens Telecommunications  
Company of Minnesota

CAH/se:85228  
enclosures

1 PU-2304-00-270 Pages: 167  
06/02/2000  
Citizens Telecommunications Company of Minn  
Application for Local Exchange PC&N

CC: Comm Legal PUD (3)

**MASLON  
EDELMAN  
BORMAN  
& BRAND**

*Limited  
Liability Partnership*

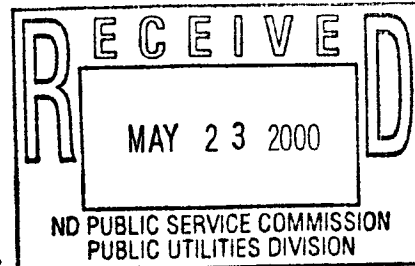
MARVIN BORMAN  
NEIL I. SELL  
WILLIAM E. MULLIN  
WILLIAM Z. PENTLOVITCH  
JOSEPH ALEXANDER  
GARY J. HAUGEN  
THOMAS H. BORMAN  
MARK BAUMANN  
DAVID F. HERR  
R. LAWRENCE PURDY  
JAMES D. O'CONNOR  
RICHARD G. WILSON  
HOWARD B. TARKOW  
WILLIAM M. MOWER, P.A.  
LARRY A. KOCH  
VIRGINIA A. BELL  
JUSTIN H. PERL  
COOPER S. ASHLEY  
SALLY STOLEN GROSSMAN  
MARTIN R. ROSENBAUM  
TERRI KRIVOSHA  
MARY E. VASALY  
JOHN W. PROVO  
EDWIN CHANIN  
CLARK T. WHITMORE  
WAYNE S. MOSKOWITZ  
CHARLES A. HOFFMAN  
MARK W. LEE  
LORRIE L. SALZL  
ALAIN M. BAUDRY  
RICHARD A. KEMPF  
SUSAN E. OLIPHANT  
JONATHAN S. PARRITZ  
KIRK O. KOLBO  
BRIAN J. KLEIN  
JAMES F. KILLIAN  
JAMES F. HANNEMAN  
SHERYL G. MORRISON  
DOUGLAS T. HOLOD  
NEIL P. AYOTTE  
ANDREW N. JACOBSON  
CYNTHIA F. GILBERTSON  
PENNY R. HEABERLIN  
LAURIE A. KINDEL  
MICHAEL C. MCCARTHY  
PHILIP J. TILTON  
R. CHRISTOPHER SUR  
SHAWN R. McINTEE  
MARGARET C. HOBDA  
HOWARD A. ROSTON  
MARGARET M. KILLIAN  
PETER J. CARLTON  
STEPHEN A. TIGHT  
MARGARET D. LUPKES  
MELISSA M. WELDON  
LAURA E. WALVOORD  
CHRISTOPHER J. MELSHA  
ALAN M. GILBERT  
KAI H. RICHTER  
LISA C. NETZER

OF COUNSEL  
MARTIN G. WEINSTEIN  
MICHAEL L. SNOW  
ROYCE N. SANNER  
SUSAN J. LINK

RETIRED  
CHARLES QUAINANCE, JR.  
ROBERT A. ENGELKE

SAMUEL H. MASLON  
1901-1988  
HYMAN EDELMAN  
1906-1993

3300 NORWEST CENTER  
90 SOUTH SEVENTH STREET  
MINNEAPOLIS, MINNESOTA 55402-4140  
(612) 672-8200  
FAX (612) 672-8397



May 23, 2000

**Via Facsimile and U.S. Mail**  
Sharon Helbling  
Public Service Commission  
600 E. Boulevard Avenue, Dept. 408  
Bismarck, ND 58505-0480

Dear Ms. Helbling:

I am writing in response to your letter dated May 9, 2000. Citizens Telecommunications Company of Minnesota does wish to proceed with its Application for Authority to provide local telecommunications services in North Dakota. However, Citizens Minnesota has determined that it does not need and will not seek authority to act as an interexchange reseller. Accordingly, I do not believe that it will be necessary to provide those forms.

I do not yet have the original Certificate of Good Standing and Application for Certificate of Authority, but will provide them to you at the earliest opportunity.

Thank you very much for your kind attention to this matter and my apologies for not responding more promptly to your letter dated February 14, 2000.

Sincerely,

A handwritten signature in black ink, appearing to read "Charles A. Hoffman".

Charles A. Hoffman

CAH/sed  
CC: Pat Fahn

84587v1



**Public Service Commission**  
State of North Dakota

COMMISSIONERS

Bruce Hagen  
President  
Susan E. Wefald  
Leo M. Reinbold

600 E Boulevard Ave. Dept. 408  
Bismarck, North Dakota 58505-0480  
e-mail: sab@oracle.psc.state.nd.us  
TDD 800-366-6888  
Fax 701-328-2410  
Phone 701-328-2400

Executive Secretary  
Jon H. Mielke

May 9, 2000

Charles A Hoffman  
Maslon Edelman Borman & Brand  
3300 Norwest Ctr 90 S 7<sup>th</sup> ST  
Minneapolis MN 55402-4140

Dear Mr. Hoffman:

On February 14, 2000 we received an application for Citizens Telecommunications Company of Minnesota for authority to provide telecommunications services in North Dakota. On February 14<sup>th</sup> I wrote you a letter (copy attached), requesting more information before we could process the applications.

Since we have heard nothing from you since that time, I am writing to find out the status of your request. Does Citizens still want to pursue certification in North Dakota, or is it going to abandon the project?

We would appreciate a response from you as soon as possible.

Thank you.

Sincerely,

A handwritten signature in cursive script that reads "Sharon Helbling".

Sharon Helbling  
Public Utilities Division

Sdh

Enclosure



**Public Service Commission**  
State of North Dakota

600 E Boulevard Ave. Dept. 408  
Bismarck, North Dakota 58505-0480  
e-mail: msmail.sab@oracle.psc.state.nd.us  
TDD 800-366-6888  
Fax 701-328-2410  
Phone 701-328-2400

COMMISSIONERS

Bruce Hagen  
President  
Susan E. Wefald  
Leo M. Reinbold

February 14, 2000

Executive Secretary  
Jon H. Mielke

Charles A Hoffman  
Maslon Edelman Borman & Brand  
3300 Norwest Ctr 90 S 7<sup>th</sup> St  
Minneapolis MN 55402-4140

Dear Mr. Hoffman:

We received your application for Citizens Telecommunications Company of Minnesota for authority to provide telecommunications services in North Dakota.

In your application you are seeking reseller authority as well. The Public Convenience and Necessity authority and reseller authority are two separate issues and they are handled separately. Therefore I am enclosing an Application for Certificate of Registration form which you need to complete for reseller authority. I have also enclosed the rules for resellers, a bond form, an example of an Escrow Agreement, and the policy on bonds for CLECs.

We also need an original Certificate of Good Standing, and copies of the Application for Certificate of Authority, and any other related corporate papers filed in North Dakota. You can obtain those documents from the North Dakota Secretary of State's office at 701-328-2900.

The above requirements must be met before we can process these applications. IF you have any questions, please call me at 701-328-4076. Thank you.

Sincerely,

A handwritten signature in black ink that reads "Sharon Helbling".

Sharon Helbling  
Public Utilities Division

Sdh

Enclosures

**MASLON  
EDELMAN  
BORMAN  
& BRAND**

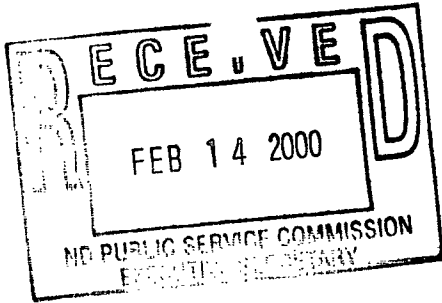
*Limited  
Liability Partnership*

MARVIN BORMAN  
NEIL I. SELL  
WILLIAM E. MULLIN  
WILLIAM Z. PENTELOVITCH  
JOSEPH ALEXANDER  
GARY J. HAUGEN  
THOMAS H. BORMAN  
MARK BAUMANN  
DAVID F. HERR  
R. LAWRENCE PURDY  
JAMES D. O'CONNOR  
RICHARD G. WILSON  
HOWARD B. TARKOW  
WILLIAM M. MOWER, P.A.  
LARRY A. KOCH  
VIRGINIA A. BELL  
JUSTIN H. PERL  
COOPER S. ASHLEY  
SALLY STOLEN GROSSMAN  
TERRI KRIVOSHA  
MARY R. VASALY  
JOHN W. PROVO  
EDWIN CHANIN  
CLARK T. WHITMORE  
WAYNE S. MOSKOWITZ  
CHARLES A. HOFFMAN  
MARK W. LEE  
LORRIE L. SALZL  
ALAIN M. BAUDRY  
RICHARD A. KEMPF  
SUSAN E. OLIPHANT  
JONATHAN S. PARRITZ  
KIRK O. KOLBO  
BRIAN J. KLEIN  
JAMES F. KILLIAN  
JAMES F. HANNEMAN  
SHERYL G. MORRISON  
DOUGLAS T. HOLOD  
NEIL P. AYOTTE  
ANDREW N. JACOBSON  
CYNTHIA F. GILBERTSON  
PENNY R. HEABERLIN  
LAURIE A. KINDEL  
MICHAEL C. MCCARTHY  
PHILIP J. TILTON  
GAY L. GREITER  
R. CHRISTOPHER SUR  
SHAWN R. McINTEE  
MARGARET C. HOBDAY  
HOWARD A. ROSTON  
MARGARET M. KILLIAN  
PETER J. CARLTON  
STEPHEN A. TIGHT  
MARGARET D. LUPKES  
MELISSA M. WELDON  
LAURA E. WALVOORD  
CHRISTOPHER J. MELSHA  
ALAN M. GILBERT  
KAI H. RICHTER

OF COUNSEL  
MARTIN G. WEINSTEIN  
MICHAEL L. SNOW  
ROYCE N. SANNER  
SUSAN J. LINK

RETIRED  
CHARLES QUAINANCE, JR.  
ROBERT A. ENGELKE

SAMUEL H. MASLON  
1901-1988  
HYMAN EDELMAN  
1906-1993



3300 NORWEST CENTER  
90 SOUTH SEVENTH STREET  
MINNEAPOLIS, MINNESOTA 55402-4140  
(612) 672-8200  
FAX (612) 672-8397

Writer's Direct Dial  
672-8368

February 11, 2000

99-1423

John Mielke  
Secretary  
North Dakota Public Service Commission  
State Capitol Building, 12<sup>th</sup> Floor  
Bismark, ND 58505

Re: Citizens Telecommunications Company of Minnesota  
Application for a Certificate of Public Convenience and  
Necessity to Provide Local Telecommunication Services

Dear Mr. Mielke:

Enclosed for filing on behalf of Citizens Telecommunications Company of Minnesota ("Citizens Minnesota") are an original and eight copies of its Application for a Certificate of Public Convenience and Necessity to Provide Local Telecommunication Services in the state of North Dakota. Please date stamp one copy and return it to the undersigned in the enclosed envelope provided.

If you have any questions concerning this filing, please do not hesitate to contact me.

Sincerely,

Charles A. Hoffman  
Counsel for Citizens Telecommunications  
Company of North Dakota

CAH/sel  
Enclosures  
68063



Minnesota to obtain such a Certificate.<sup>1</sup> This Application presents the information the Commission requires to determine that Citizens Minnesota meets the statutory requirements of N.D.C.C. § 49-03.1-04.<sup>2</sup>

**A. DESCRIPTION OF APPLICANT.**

Citizens Minnesota is a wholly owned subsidiary of Citizens, a diversified public utility that, through its various operating divisions or subsidiaries, currently provides telecommunications, electric, gas, water and wastewater services to approximately 1.9 million customers in 22 states. A certified copy of Citizens' Certificate of Incorporation is attached as Exhibit 1. Citizens provides these services through divisions and subsidiaries divided into two business sectors: (1) the Public Services Sector, which includes electric, gas, water and wastewater services,<sup>3</sup> and (2) the Communications Sector, which provides both regulated and competitive communication services to residential, business, and wholesale customers. Through subsidiaries, Citizens currently operates as an incumbent local exchange carrier ("ILEC") in thirteen states and provides local, intra-Lata and long-distance services to approximately one million access lines.<sup>4</sup> Citizens also owns 83% of Electric Lightwave, Inc., a leading full-service, facilities-based, competitive local exchange carrier.

---

<sup>1</sup>Citizens Minnesota is uncertain whether GTE has a Certificate from North Dakota. If it does, Citizens Minnesota seeks a transfer of that Certificate. If it does not, Citizens Minnesota requests that a new Certificate be issued.

<sup>2</sup>N.D.C.C. § 49-03.1-04 requires the Commission to consider (1) the need for the service; (2) the fitness and ability of the applicant to provide service; (3) the effect on other public utilities providing similar service; (4) the adequacy of the proposed service; and (5) the technical, financial, and managerial ability of the applicant to provide service.

<sup>3</sup>As this Commission knows, Citizens has already agreed to sell its water utilities and is in the process of seeking buyers for its other non-communications properties.

<sup>4</sup>Citizens currently owns local exchange subsidiaries in Arizona, California, Idaho, Montana, Nevada, New Mexico, New York, Oregon, Pennsylvania, Tennessee, Utah, West Virginia and Wisconsin.

Citizens' business strategy is to focus on and expand the Communications Sector's operations. As part of that strategy, Citizens and GTE (or its affiliates) entered into a series of agreements on May 27, 1999, under which Citizens will purchase all of GTE's properties in Minnesota (approximately 117 exchanges, serving approximately 130,000 customers), and additional properties in Arizona and California. Exhibit 2 contains a certified copy of Citizens' Board of Directors' Resolutions approving the acquisitions from GTE. Citizens expects to temporarily fund these transactions with either cash and investment balances, or bank credit facilities. Permanent funding will come from the sale or other disposition of Citizens' gas, electric and water properties. Citizens does not presently expect any need to issue any long term securities as a result of these purchases.

In 1998, Citizens had annual operating revenues of \$1.542 billion. It has a strong income statement and balance sheet, with long-term debt rated A+ by Standard & Poor's Corporation and A2 by Moody's Investors Service. More detailed information about Citizens financial strength and stability may be found in the attached most recent Annual Report and SEC Forms 10K and 10Q (Exhibits 5 and 6).

**B. SERVICE ADDRESSES**

Notices and other pleadings in connection with this Application should be served on Citizens and its counsel as follows:

For Citizens Minnesota

Aloa Stevens  
Government Affairs-West  
Citizens Communications  
5600 Headquarters Drive  
Plano, Texas 75024

Lance Tade  
Citizens Communications  
9672 South  
700 East Suite 101  
Sandy, UT 84070-3555

Craig A. Marks  
Citizens Utilities Company  
2901 North Central Avenue, Suite 1660  
Phoenix, Arizona 85012

Charles A. Hoffman  
Maslon Edelman Borman & Brand LLP  
3300 Norwest Tower  
90 South Seventh Street  
Minneapolis, MN 55402

## **II. REASONS FOR THE TRANSACTION**

Citizens is engaging in this transaction because, over the long-term, it believes that the transaction will allow it to better achieve its goals in the increasingly competitive telecommunications environment. The changing nature of the telecommunications industry within the United States makes it desirable for Citizens to focus upon its area of greatest strength. Citizens has decided to focus primarily on its communications businesses. Citizens has determined that it must increase the size of its telecommunications operations to compete with alternate providers currently in and soon to enter the marketplace. Its ultimate goal is to grow its local exchange business to three million access lines over the next several years. Citizens has entered into transactions with GTE and U S WEST as part of its strategy to acquire and operate telecommunications businesses in small and medium-size cities and towns that are experiencing above-average economic and population growth. The properties Citizens will acquire from GTE complement many of Citizens' existing operations. As Citizens' CEO Leonard Tow has stated:

"Providing small and medium-size cities and towns in America with the most advanced technology, products and services is the key to superior growth in the telecommunications business for Citizens in the new millennium."

### **III. PUBLIC CONVENIENCE AND NECESSITY**

#### **A. QUALIFICATIONS OF APPLICANT.**

A necessary condition of Citizens Minnesota acquiring and operating the GTE property is this Commission's granting Citizens Minnesota a Certificate of Public Convenience and Necessity relative to those North Dakota customers served out of the Oslo, Minnesota exchange. Citizens respectfully requests the following actions by the Commission.

1. Granting Citizens Minnesota a Certificate of Convenience and Public Necessity to provide essential and non-essential local services as well as facilities based intraLATA toll service in North Dakota for the customers served out of the Oslo exchange in Minnesota.
2. Granting Citizens Minnesota Eligible Telecommunications Carrier ("ETC") status for this territory.
3. Indicating to the FCC the Commission's approval (or non-opposition) to a waiver/modification of the Part 36 study area for North Dakota to reflect this transaction.

Citizens and its subsidiary, Citizens Minnesota, clearly meet all technical, managerial, financial and legal qualifications required of applicants for a Certificate of Convenience and Necessity. Citizens Minnesota will draw heavily on the management resources of Citizens' Communications Sector for planning, marketing, network, service development, provisioning and delivery and legal/regulatory assistance. The above description of Citizens establishes that its subsidiaries have broad experience in providing local exchange telecommunications services across the United States. Furthermore,

Citizens' subsidiaries have received authority to provide local exchange services in 13 states, and have fully met the licensing requirements of each of those states.

Descriptions of the backgrounds of Citizens' management, which demonstrate the extensive telecommunications experience and expertise of Citizens Minnesota management team, are contained in Citizens' Annual Report and its annual report to the Securities and Exchange Commission on Form 10K for the year ending December 31, 1998. Copies of those documents are attached hereto as Exhibit 6. Also attached as Exhibit 7 is an organizational chart of Citizens and its various subsidiaries. Attached as Exhibits 8, 9 and 10 are, respectively, Citizens' Certificate of Authority, Certificate of Good Standing (original) and Certificate of Trade Name Registration.

#### **B. SERVICES TO BE PROVIDED AND THEIR ADEQUACY**

Citizens and GTE are working together to ensure that the transfer of assets from GTE to Citizens Minnesota will be seamless and transparent to all customers, including those in North Dakota. Citizens currently expects that the Citizens-GTE transaction will be approved by the Minnesota Commission in early July, 2000.<sup>2</sup> Citizens Minnesota believes that the services it proposes to provide in the acquired exchanges will not only provide adequate service to its consumers, but will in the long run provide advanced service as Citizens Minnesota implements its business plan. Among the benefits of the services Citizens Minnesota will provide are:

1. High Quality Services: Citizens Minnesota is committed to operating a high quality network for its customers. Citizens has a strong history of investing to meet the needs of its customers. Since 1993, Citizens has acquired more than 657,000 access lines from other local phone companies. Citizens' subsidiaries currently operate all-digital, local exchange properties in 13 states:

---

<sup>2</sup>A copy of the Minnesota Commission's Order approving the transaction will be provided when it becomes available.

Arizona, California, Idaho, Montana, Nevada, New Mexico, New York Oregon, Pennsylvania, Tennessee, Utah, West Virginia and Wisconsin. Citizens stands ready to invest capital in its rural and suburban properties to upgrade existing technology. While exact details are still being developed, Citizens Minnesota has informed the Minnesota Commission that it expects to invest in excess of \$24 million over the next three years in the acquired exchanges.

2. Long Distance and Other Services: Citizens intends to provide a full range of services to its North Dakota communications customers. Services will include local and long-distance offerings, and may expand to include other advanced services. Citizens Communications currently contracts with AT&T to provide the nationwide network for its long-distance products, which include fax/data communications, 800/888 service, international calling, calling cards and direct dial.

3. Competitive Rates as a Result of Cost Savings: Initially, Citizens Minnesota will adopt GTE's existing tariff rates.

4. Corporate Citizenship: Citizens provides benefits to its employees consistent with those provided by leading U.S. companies, and supports its local communities. Citizens has always strived to be a valued corporate citizen in the communities it serves and will continue that tradition.

5. Customer Relations: Citizens values its customers and is committed to providing top quality customer relations. Citizens Communications currently expects to expand its Johnstown, New York and Sherburne, New York call centers to handle new service and repair calls originating in the Minnesota exchange. This service change should be transparent to customers.

Citizens Minnesota will work with the Commission staff to develop a customer education outreach to ensure a smooth transition from GTE to Citizens Minnesota. This will include

newspaper advertising and bill inserts as appropriate. Through this outreach effort, customers will be informed of new service and repair numbers and other important information needed as a result of the transition.

6. No Material Impact on Employment: The transaction is not expected to have a material impact on employment levels in North Dakota.

7. Continued Regulatory Compliance: Citizens Minnesota will abide by all applicable statutes and rules of this Commission.

**C. NEED FOR THE SERVICE.**

As noted above, Citizens Minnesota intends to provide high quality services to the customers served out of the Oslo Minnesota exchange, and to ensure a seamless transition from GTE to Citizens Minnesota for these customers.

**D. EFFECT ON OTHER UTILITIES.**

Citizens Minnesota anticipates that there will be little, if any, impact on other utilities since it is purchasing existing exchanges. Citizens Minnesota expects to be an active participant in the newly competitive local exchange market.

**IV. DESIGNATION AS ELIGIBLE TELECOMMUNICATIONS CARRIER**

Citizens has requested that this Commission certify it as an Eligible Telecommunications Carrier (ETC) for this territory. The basic requirement for eligibility as an ETC requires that Citizens (1) offer the services that are supported by federal universal service support mechanisms and offer the services designated by the FCC for such federal support mechanisms for schools,

libraries and health care providers; and (2) advertise the availability of such services and the charges therefore using media of general distribution.

In all states where Citizens currently operates as a local exchange carrier (LEC) and in the North Dakota/Minnesota exchange at issue in this Application, Citizens does (or will) offer the telecommunication services which are supported by federal universal service support mechanisms, including (but not limited to) voice grade access to the public switch network, local usage, dual tone multi-frequency signally or its functional equivalent, single party service or its functional equivalent, access to emergency services, access to operator services, access to interexchange service, access to directory assistance, and toll limitation for qualifying low income consumers. Each of these services will be offered in the affected exchange in a manner adequate to meet the requirements of all applicable FCC orders. In addition, for schools and libraries, and for health care providers, Citizens will provide the services supported by universal service support mechanisms. Citizens will advertise the availability of all universal services and the charges therefor using media of general distribution. Citizens will adhere to applicable FCC and state commission requirements for such advertising.

In sum, Citizens believes that it has in all states where it operates, and will in the affected exchange, meet all of the state and federal requirements for designation as an ETC provider.

## **EXHIBITS**

In further support of this application, the Applicant submits the following exhibits:

### **ACQUISITION & CORPORATE**

#### **Exhibit**

1. Articles/Certificate of Incorporation certified by Secretary of State of Delaware (Citizens Utilities Company).
2. Resolutions of Board of Directors of Citizens Utilities Company Approving Purchase of Assets certified by Corporate Secretary
3. Certificate of Incorporation (Citizens Telecommunications Company of Minnesota).
4. Application for Certificate of Authority to do Business.

### **FINANCIAL**

5. 1998 Annual Report and 10K
6. 1999 2Q 10Q

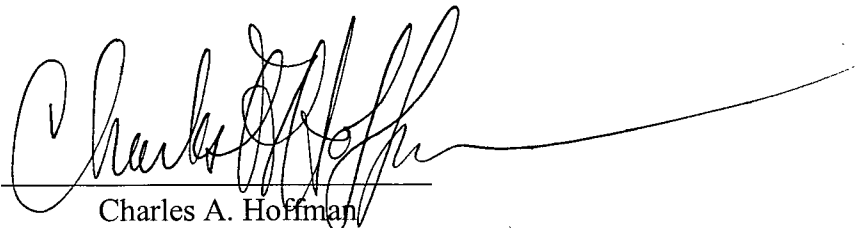
### **MISCELLANEOUS**

7. Citizens Utilities Company
8. Citizens' Certificate of Authority
9. Certificate of Good Standing (original)
10. Certificate of Trade Name Registration

WHEREFORE, Citizens Telecommunications Company of Minnesota respectfully request that the Commission grant it a Certificate of Public Convenience and Necessity as outlined herein, and allow such further relief as is necessary, including the granting of ETC status to Citizens Minnesota for the affected exchange and indicating in its Order that it does not object to the FCC's granting of study area waivers for the affected exchanges or to the reconfiguration of study area boundaries as a result of the transfer of these exchanges to Citizens.

Respectfully submitted,

Dated: May 25, 2000

By:   
Charles A. Hoffman

**MASLON EDELMAN BORMAN & BRAND  
LLP**

3300 Norwest Center  
90 South Seventh Street  
Minneapolis, MN 55402-4140  
(612) 672-8368 - Telephone  
(612) 672-8397 - Facsimile

**ATTORNEYS FOR  
CITIZENS UTILITIES COMPANY**

VERIFICATION

I, Craig A. Marks, declare under penalty of perjury that I am Associate General Counsel of Citizens Utilities Company and its subsidiary Citizens Telecommunications Company of North Dakota, the applicant in this proceeding; that I have read the foregoing application and exhibits; and that the same are true and correct to the best of my knowledge, information, or belief.

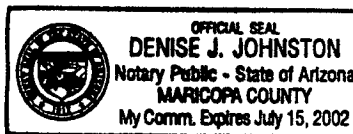
I declare under penalty of perjury that the foregoing is true and correct. Executed this 1st day of ~~May~~ <sup>June</sup>, 2000.

Craig A. Marks  
Craig A. Marks  
Associate General Counsel

Sworn and subscribed to before me  
this 1 day of ~~May~~ <sup>June</sup>, 2000.

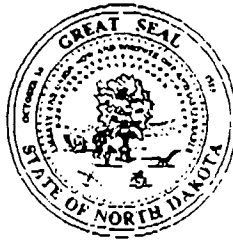
Denise J. Johnston  
Notary Public

My Commission Expires: \_\_\_\_\_



# State of North Dakota

## SECRETARY OF STATE



### CERTIFICATE OF AUTHORITY

OF

CITIZENS TELECOMMUNICATIONS COMPANY OF MINNESOTA,  
INC.

The undersigned, as Secretary of State of the State of North Dakota, hereby certifies that an application of  
CITIZENS TELECOMMUNICATIONS COMPANY OF MINNESOTA,  
INC.  
for a Certificate of Authority to transact business in this State, duly signed and verified pursuant to the provisions of the North Dakota Century Code, have been received in this office and are found to conform to law.

ACCORDINGLY the undersigned, as such Secretary of State, and by virtue of the authority vested in him by law, hereby issues this Certificate of Authority to  
CITIZENS TELECOMMUNICATIONS COMPANY OF MINNESOTA,  
INC.  
to transact business in this State under the name of  
CITIZENS TELECOMMUNICATIONS COMPANY OF MINNESOTA,  
INC.

Issued: May 12, 2000

A handwritten signature in cursive script, reading "Alvin A. Jaeger".

Alvin A. Jaeger  
Secretary of State

EXHIBIT 8

# *State of North Dakota*

## SECRETARY OF STATE



### CERTIFICATE OF GOOD STANDING

OF

CITIZENS TELECOMMUNICATIONS COMPANY OF MINNESOTA,  
INC.

The undersigned, as Secretary of State of the State of North Dakota, hereby certifies that CITIZENS TELECOMMUNICATIONS COMPANY OF MINNESOTA, INC. , a Delaware corporation, authorized to transact business in the State of North Dakota on May 12, 2000, and according to the records of this office as of this date, has paid all fees due this office as required by North Dakota statutes governing foreign corporations.

ACCORDINGLY the undersigned, as such Secretary of State, and by virtue of the authority vested in him by law, hereby issues this Certificate of Good Standing to

CITIZENS TELECOMMUNICATIONS COMPANY OF MINNESOTA,  
INC.

Issued: May 24, 2000

A handwritten signature in cursive script, reading "Alvin A. Jaeger".

Alvin A. Jaeger  
Secretary of State

EXHIBIT 9

# State of North Dakota

## SECRETARY OF STATE



### CERTIFICATE OF TRADE NAME REGISTRATION OF

CITIZENS COMMUNICATIONS COMPANY OF MINNESOTA

The undersigned, as Secretary of State of North Dakota, hereby certifies that an Application for Registration of a Trade Name, duly signed pursuant to the provisions of the North Dakota Trade Names statutes, has been received in this office and is found to conform to law.

Accordingly the undersigned, as such Secretary of State, and by virtue of the authority vested in him by law, hereby issues the Certificate of Trade Name Registration of CITIZENS COMMUNICATIONS COMPANY OF MINNESOTA which is owned by CITIZENS TELECOMMUNICATIONS COMPANY OF MINNESOTA, INC. with an address of THREE HIGH RIDGE PARK , STAMFORD, CT 06905-1328.

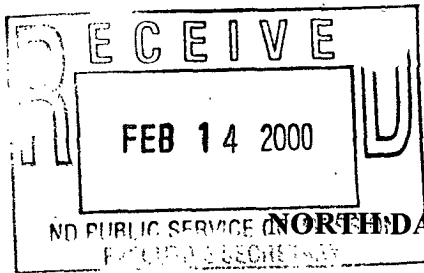
The Trade Name Registration shall remain in force until May 12, 2005.

DATED: May 12, 2000

A handwritten signature in cursive script, appearing to read "Alvin A. Jaeger".

Alvin A. Jaeger  
Secretary of State

EXHIBIT 10



BEFORE THE  
NORTH DAKOTA PUBLIC SERVICE COMMISSION

In the Matter of the Application of )  
)  
CITIZENS TELECOMMUNICATIONS )  
COMPANY OF MINNESOTA )  
)  
For Authority to Operate as an )  
Incumbent Local Exchange )  
Provider in North Dakota )

Case No. \_\_\_\_\_

**APPLICATION OF CITIZENS TELECOMMUNICATION COMPANY OF  
MINNESOTA**

Citizens Telecommunications Company of Minnesota ("Citizens Minnesota"), by its undersigned counsel, hereby requests, pursuant to N.D.C.C. Chapter 49-03.1, that the North Dakota Public Service Commission (the "Commission") grant it a Certificate of Public Convenience and Necessity. This request is a result of Citizens Utilities Company's recent agreement to purchase certain exchanges owned and operated by Contel of Minnesota, Inc. d/b/a GTE Minnesota ("GTE"). Some customers served by these exchanges reside in North Dakota.

**I. DISCUSSION**

On May 27, 1999, Citizens Utilities Company ("Citizens") and GTE entered into an agreement for the purchase and sale of telephone exchanges whereby Citizens agreed to purchase all of GTE's exchanges in the State of Minnesota (the "Agreement"). The entity providing service in Minnesota will be Citizens Minnesota. One of the GTE exchanges in Minnesota (Oslo) provides service to certain customers in North Dakota. Because Citizens Minnesota does not presently provide telephone service within the state of North Dakota, and consequently has not been granted a Certificate of Public Convenience and Necessity by this Commission, it is necessary for Citizens

Minnesota to obtain such a Certificate.<sup>1</sup> This Application presents the information the Commission requires to determine that Citizens Minnesota meets the statutory requirements of N.D.C.C. § 49-03.1-04.<sup>2</sup>

**A. DESCRIPTION OF APPLICANT.**

Citizens Minnesota is a wholly owned subsidiary of Citizens, a diversified public utility that, through its various operating divisions or subsidiaries, currently provides telecommunications, electric, gas, water and wastewater services to approximately 1.9 million customers in 22 states. A certified copy of Citizens' Certificate of Incorporation is attached as Exhibit 1. Citizens provides these services through divisions and subsidiaries divided into two business sectors: (1) the Public Services Sector, which includes electric, gas, water and wastewater services,<sup>3</sup> and (2) the Communications Sector, which provides both regulated and competitive communication services to residential, business, and wholesale customers. Through subsidiaries, Citizens currently operates as an incumbent local exchange carrier ("ILEC") in thirteen states and provides local, intra-Lata and long-distance services to approximately one million access lines.<sup>4</sup> Citizens also owns 83% of Electric Lightwave, Inc., a leading full-service, facilities-based, competitive local exchange carrier.

---

<sup>1</sup>Citizens Minnesota is uncertain whether GTE has a Certificate from North Dakota. If it does, Citizens Minnesota seeks a transfer of that Certificate. If it does not, Citizens Minnesota requests that a new Certificate be issued.

<sup>2</sup>N.D.C.C. § 49-03.1-04 requires the Commission to consider (1) the need for the service; (2) the fitness and ability of the applicant to provide service; (3) the effect on other public utilities providing similar service; (4) the adequacy of the proposed service; and (5) the technical, financial, and managerial ability of the applicant to provide service.

<sup>3</sup>As this Commission knows, Citizens has already agreed to sell its water utilities and is in the process of seeking buyers for its other non-communications properties.

<sup>4</sup> Citizens currently owns local exchange subsidiaries in Arizona, California, Idaho, Montana, Nevada, New Mexico, New York, Oregon, Pennsylvania, Tennessee, Utah, West Virginia and Wisconsin.

Citizens' business strategy is to focus on and expand the Communications Sector's operations. As part of that strategy, Citizens and GTE (or its affiliates) entered into a series of agreements on May 27, 1999, under which Citizens will purchase all of GTE's properties in Minnesota (approximately 117 exchanges, serving approximately 130,000 customers), and additional properties in Arizona and California. Exhibit 2 contains a certified copy of Citizens' Board of Directors' Resolutions approving the acquisitions from GTE. Citizens expects to temporarily fund these transactions with either cash and investment balances, or bank credit facilities. Permanent funding will come from the sale or other disposition of Citizens' gas, electric and water properties. Citizens does not presently expect any need to issue any long term securities as a result of these purchases.

In 1998, Citizens had annual operating revenues of \$1.542 billion. It has a strong income statement and balance sheet, with long-term debt rated A+ by Standard & Poor's Corporation and A2 by Moody's Investors Service. More detailed information about Citizens financial strength and stability may be found in the attached most recent Annual Report and SEC Forms 10K and 10Q (Exhibits 5 and 6).

**B. SERVICE ADDRESSES**

Notices and other pleadings in connection with this Application should be served on Citizens and its counsel as follows:

For Citizens Minnesota

Aloa Stevens  
Government Affairs-West  
Citizens Communications  
5600 Headquarters Drive  
Plano, Texas 75024

Lance Tade  
Citizens Communications  
9672 South  
700 East Suite 101  
Sandy, UT 84070-3555

Susan M. Mikes  
Associate General Counsel  
Citizens Utilities Company  
3 High Ridge Park  
Stamford, CT 06905

Charles A. Hoffman  
Maslon Edelman Borman & Brand LLP  
3300 Norwest Tower  
90 South Seventh Street  
Minneapolis, MN 55402

## **II. REASONS FOR THE TRANSACTION**

Citizens is engaging in this transaction because, over the long-term, it believes that the transaction will allow it to better achieve its goals in the increasingly competitive telecommunications environment. The changing nature of the telecommunications industry within the United States makes it desirable for Citizens to focus upon its area of greatest strength. Citizens has decided to focus primarily on its communications businesses. Citizens has determined that it must increase the size of its telecommunications operations to compete with alternate providers currently in and soon to enter the marketplace. Its ultimate goal is to grow its local exchange business to three million access lines over the next several years. Citizens has entered into transactions with GTE and U S WEST as part of its strategy to acquire and operate telecommunications businesses in small and medium-size cities and towns that are experiencing above-average economic and population growth. The properties Citizens will acquire from GTE complement many of Citizens' existing operations. As Citizens' CEO Leonard Tow has stated:

"Providing small and medium-size cities and towns in America with the most advanced technology, products and services is the key to superior growth in the telecommunications business for Citizens in the new millennium."

### **III. PUBLIC CONVENIENCE AND NECESSITY**

#### **A. QUALIFICATIONS OF APPLICANT.**

A necessary condition of Citizens Minnesota acquiring and operating the GTE property is this Commission's granting Citizens Minnesota a Certificate of Public Convenience and Necessity relative to those North Dakota customers served out of the Oslo, Minnesota exchange.. Citizens respectfully requests the following actions by the Commission.

1. Granting Citizens Minnesota a Certificate of Convenience and Public Necessity to provide essential and non-essential local services as well as facilities based intraLATA toll service in North Dakota for the customers served out of the Oslo exchange in Minnesota.
2. Issuing Citizens Minnesota a Certificate of Registration to act as a reseller of interLATA toll services.
3. Granting Citizens Minnesota Eligible Telecommunications Carrier ("ETC") status for this territory.
4. Indicating to the FCC the Commission's approval (or non-opposition) to a waiver/modification of the Part 36 study area for North Dakota to reflect this transaction.

Citizens and its subsidiary, Citizens Minnesota, clearly meet all technical, managerial, financial and legal qualifications required of applicants for a Certificate of Convenience and Necessity. Citizens Minnesota will draw heavily on the management resources of Citizens' Communications Sector for planning, marketing, network, service development, provisioning and delivery and legal/regulatory assistance. The above description of Citizens establishes that its subsidiaries have broad experience in providing local exchange telecommunications services across the United States. Furthermore,

Citizens' subsidiaries have received authority to provide local exchange services in 13 states, and have fully met the licensing requirements of each of those states.

Descriptions of the backgrounds of Citizens' management, which demonstrate the extensive telecommunications experience and expertise of Citizens Minnesota management team, are contained in Citizens' Annual Report and its annual report to the Securities and Exchange Commission on Form 10K for the year ending December 31, 1998. Copies of those documents are attached hereto as Exhibit 6. Also attached as Exhibit 7 is an organizational chart of Citizens and its various subsidiaries.

**B. SERVICES TO BE PROVIDED AND THEIR ADEQUACY**

Citizens and GTE are working together to ensure that the transfer of assets from GTE to Citizens Minnesota will be seamless and transparent to all customers, including those in North Dakota. Citizens currently expects that the Citizens-GTE transaction will be approved by the Minnesota Commission on or about May 1, 2000. Citizens Minnesota believes that the services it proposes to provide in the acquired exchanges will not only provide adequate service to its consumers, but will in the long run provide advanced service as Citizens Minnesota implements its business plan. Among the benefits of the services Citizens Minnesota will provide are:

1. High Quality Services: Citizens Minnesota is committed to operating a high quality network for its customers. Citizens has a strong history of investing to meet the needs of its customers. Since 1993, Citizens has acquired more than 657,000 access lines from other local phone companies. Citizens' subsidiaries currently operate all-digital, local exchange properties in 13 states: Arizona, California, Idaho, Montana, Nevada, New Mexico, New York Oregon, Pennsylvania, Tennessee, Utah, West Virginia and Wisconsin. Citizens stands ready to invest capital in its rural

and suburban properties to upgrade existing technology. While exact details are still being developed, Citizens Minnesota has informed the Minnesota Commission that it expects to invest in excess of \$24 million over the next three years in the acquired exchanges.

2. Long Distance and Other Services: Citizens intends to provide a full range of services to its North Dakota communications customers. Services will include local and long-distance offerings, and may expand to include other advanced services. Citizens Communications currently contracts with AT&T to provide the nationwide network for its long-distance products, which include fax/data communications, 800/888 service, international calling, calling cards and direct dial.

3. Competitive Rates as a Result of Cost Savings: Initially, Citizens Minnesota will adopt GTE's existing tariff rates.

4. Corporate Citizenship: Citizens provides benefits to its employees consistent with those provided by leading U.S. companies, and supports its local communities. Citizens has always strived to be a valued corporate citizen in the communities it serves and will continue that tradition.

5. Customer Relations: Citizens values its customers and is committed to providing top quality customer relations. Citizens Communications currently expects to expand its Johnstown, New York and Sherburne, New York call centers to handle new service and repair calls originating in the Minnesota exchange. This service change should be transparent to customers.

Citizens Minnesota will work with the Commission staff to develop a customer education outreach to ensure a smooth transition from GTE to Citizens Minnesota. This will include newspaper advertising and bill inserts as appropriate. Through this outreach effort, customers will

be informed of new service and repair numbers and other important information needed as a result of the transition.

6. No Material Impact on Employment: The transaction is not expected to have a material impact on employment levels in North Dakota.

7. Continued Regulatory Compliance: Citizens Minnesota will abide by all applicable statutes and rules of this Commission.

**C. NEED FOR THE SERVICE.**

As noted above, Citizens Minnesota intends to provide high quality services to the customers served out of the Oslo Minnesota exchange, and to ensure a seamless transition from GTE to Citizens Minnesota for these customers.

**D. EFFECT ON OTHER UTILITIES.**

Citizens Minnesota anticipates that there will be little, if any, impact on other utilities since it is purchasing existing exchanges. Citizens Minnesota expects to be an active participant in the newly competitive local exchange market.

## **EXHIBITS**

In further support of this application, the Applicant submits the following exhibits:

### **ACQUISITION & CORPORATE**

#### **Exhibit**

1. Articles/Certificate of Incorporation certified by Secretary of State of Delaware (Citizens Utilities Company).
2. Resolutions of Board of Directors of Citizens Utilities Company Approving Purchase of Assets certified by Corporate Secretary
3. Certificate of Incorporation (Citizens Telecommunications Company of Minnesota).
4. Application for Certificate of Authority to do Business.

### **FINANCIAL**

5. 1998 Annual Report and 10K
6. 1999 2Q 10Q

### **MISCELLANEOUS**

#### **Corporate Structure Chart**

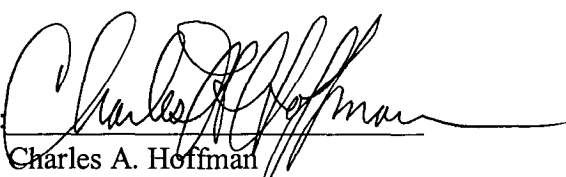
7. Citizens Utilities Company

WHEREFORE, Citizens Telecommunications Company of Minnesota respectfully request that the Commission grant it a Certificate of Public Convenience and Necessity as outlined herein, and allow such further relief as is necessary, including the granting of ETC status to Citizens Minnesota for the affected exchange and indicating in its Order that it does not

object to the FCC's granting of study area waivers for the affected exchanges or to the reconfiguration of study area boundaries as a result of the transfer of these exchanges to Citizens.

Respectfully submitted,

Dated: February 10, 2000

By:   
Charles A. Hoffman

Maslon Edelman Borman & Brand LLP  
3300 Norwest Center  
90 South Seventh Street  
Minneapolis, MN 55402-4140  
(612) 672-8368 - Telephone  
(612) 672-8397 - Facsimile

**ATTORNEYS FOR  
CITIZENS UTILITIES COMPANY**

Office of the Secretary of State PAGE 1

---

I, EDWARD J. FREEL, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY THE ATTACHED IS A TRUE AND CORRECT COPY OF THE RESTATED CERTIFICATE OF "CITIZENS UTILITIES COMPANY", FILED IN THIS OFFICE ON THE EIGHTEENTH DAY OF JUNE, A.D. 1996, AT 9 O'CLOCK A.M.



*Edward J. Freel*

Edward J. Freel, Secretary of State

0345219 8100  
991376646

AUTHENTICATION: 9962017 Exhibit 1  
DATE: 09-09-99

**RESTATED CERTIFICATE OF INCORPORATION  
OF  
CITIZENS UTILITIES COMPANY**

\*\*\*\*\*

**CITIZENS UTILITIES COMPANY, a corporation organized and existing under the laws of the State of Delaware (the "Company"), hereby certifies as follows:**

**1. The name of the corporation is**

**CITIZENS UTILITIES COMPANY**

**The date of filing its original Certificate of Incorporation with the Secretary of State was November 12, 1935.**

**2. The provisions of the Amended and Restated Certificate of Incorporation of the Company as heretofore amended, are hereby amended and restated and integrated into the single instrument which is hereinafter set forth, and which is entitled Amended and Restated Certificate of Incorporation of Citizens Utilities Company without any further amendments and without any further discrepancy between the provisions of the Amended and Restated Certificate of Incorporation as heretofore amended and the provisions of the said single instrument hereinafter set forth.**

**3. The amendments and the restatement of the Amended and Restated Certificate of Incorporation herein certified have been duly adopted by the stockholders and the Board of Directors, respectively, of the Company in accordance with the provisions of Section 242 and of Section 245 of the General Corporation Law of the State of Delaware.**

**4. The capital of the Company will not be reduced under or by reason of any amendment in this Amended and Restated Certificate of Incorporation hereinafter set forth.**

**5. The text of the Amended and Restated Certificate of Incorporation shall upon the effective date of this Amended and Restated Certificate of Incorporation read as follows:**

STATE OF DELAWARE  
SECRETARY OF STATE  
DIVISION OF CORPORATIONS  
FILED 09:00 AM 06/18/1996  
960176941 - 345219

**AMENDED AND RESTATED CERTIFICATE OF INCORPORATION  
OF  
CITIZENS UTILITIES COMPANY**

**FIRST:** The name of this corporation is  
**CITIZENS UTILITIES COMPANY.**

**SECOND:** Its principal office in the State of Delaware is to be located at 1013 Centre Road, in the City of Wilmington, County of New Castle, and its resident agent is The Prentice-Hall Corporation System, Inc.

**THIRD:** The nature of the business and the objects and purposes to be transacted, promoted, and carried on are to do any or all of the things herein mentioned as fully and to the same extent as natural persons might or could do, and in any part of the world, viz.:

(a) To purchase or otherwise acquire, own, operate and dispose of all or any part of the business and properties of persons, partnerships, associations, and other corporations engaged in any business, including that of operating public utilities, and to make payment therefor by the issuance of securities of this corporation or in any other manner permitted by law, and in connection therewith to assume any or all of the bonds, mortgages, franchises, leases, contracts, indebtedness, liabilities, and obligations of such corporations, and to do any things necessary or expedient in connection therewith or with the carrying out of any plan of reorganization of predecessor company or any modification therefor.

(b) To generate, produce, buy, or in any manner acquire, and to sell, dispose of, and distribute electricity for light, heat, power, and other purposes and to carry on the business of furnishing, supplying, manufacturing, and vending light, heat, power, gas, water, steam heat, ice, refrigeration, and any and all businesses incident thereto, and to build, construct, develop, improve, acquire, hold, own, lease, maintain, and operate plants, facilities, and works for the manufacture, generation, production, accumulation, transmission, and distribution of electric energy, gas and steam, for light, power, heat and other purposes, and to acquire, construct, maintain, and operate systems of water works, gas works, steam heating plants, for the supply of water, gas, and steam heat, and to exercise rights of condemnation and eminent domain in connection with the doing of its business objects and purposes as herein set forth so far as may be permissible by law; to acquire, maintain, operate, and exercise all the rights of ownership of any telephone, telegraph, and/or other communication system or systems.

(c) To build, construct, develop, improve, acquire, hold, own, lease, maintain and operate, by electricity or other power, street railways and interurban railways for the transportation of passengers, mail, express, merchandise, or other freight in any part of the world.

(d) To produce, mine, buy, sell, store, market, deal in, and prospect for coal and minerals of all kinds and the products and by-products thereof.

(e) To organize, incorporate, reorganize, finance, and to aid and assist financially or otherwise, companies, corporations, joint stock companies, syndicates, partnerships, and associations of all kinds, and to underwrite, subscribe for, and endorse the bonds, stocks, securities, debentures, notes, or undertakings of any such company, corporation, joint stock company, syndicate partnership or association, and to make any guarantee in connection therewith or otherwise for the payment of money or for the performance of any obligation or undertaking, and to do any and all things necessary or convenient to carry any of such purposes into effect.

(f) To carry on the business of engineering and contracting in all of its branches; to appraise, value, design, build, construct, enlarge, develop, improve, extend, and repair works, plants, systems, lines, stations, buildings, structures, mines, shafts, tunnels, wells, canals, viaducts, highways, facilities, apparatus, machinery, equipment, appliances and appurtenances, of any and every nature and kind whatsoever.

(g) To purchase and acquire securities, assets, and property of every kind and description at judicial, judiciary, trustee's, pledgee's, mortgagee's or liquidating or public or private sales, either pursuant to a plan of reorganization or otherwise, and to carry on a general salvage, liquidation, and realization business; and also to do a general commission and brokerage business.

(h) To hold in trust, issue on commission, make advances upon or sell, lease, license, transfer, organize, reorganize, incorporate, or dispose of any of the undertakings or resulting investments aforesaid, or the stock or securities thereof; to act as agent or depositary for any of the above or like purposes or any purpose herein mentioned, and to act as fiscal agent of any other person, firm or corporation.

(i) To obtain the grant of, purchase, lease, or otherwise acquire any concessions, rights, options, patents, privileges, lands, rights of way, sites, properties, undertakings or businesses, or any right, option or contract in relation thereto, and to perform, carry out, and fulfill the terms and conditions thereof and to carry the same into effect, and to develop, maintain, lease, sell, transfer, dispose of, and otherwise deal with the same.

(j) From time to time to apply for, obtain the grant of, purchase or acquire by assignment, transfer or otherwise, and to exercise, carry out and enjoy any license, power, authority, franchise, ordinance, order, right or privilege, which any government or authority, supreme, municipal or local, or any corporation or other public body shall enact, make, or grant.

(k) To issue shares of the capital, stock, bonds, debentures, debenture stock, notes, and other obligations of this corporation for cash, for labor done, for property, real or personal, or leases thereof, or for any combination of any of the foregoing, or for services rendered or in exchange for the stock debentures, debenture stock, bonds, securities, or obligations of any person, firm, association, corporation, or other organization.

(l) To purchase, acquire, and lease, and to sell, lease, and dispose of water, water rights, water records, power privileges, and appropriations for power, light, heat, mining, milling, irrigation, agricultural, domestic or any other use or purpose.

(m) To acquire by purchase, lease, own, hold, sell, mortgage, and encumber both improved and unimproved real estate wherever situate; to survey, subdivide, plat, colonize, and improve the same for the purposes of sale or otherwise; and to construct and erect thereon factories, works, plants, shops, stores, mills, hotels, houses, buildings, and other structures, and to own, use, maintain, manage, and operate the same or any thereof.

(n) To own and control and acquire, by lease, purchase, construction, or otherwise, steamships, boats, barges, hydroplanes, and vessels of all kinds or interests therein and to operate the same either on Alaska Waters and on the Waters of Puget Sound and on all navigable rivers and waters connected therewith and elsewhere, or both, for the transportation of passengers and freight of all kinds, with power to purchase, build, construct, repair, lease, sell, convey, and operate vessels of all kinds, and all machinery, appliances and apparatus incident, necessary or convenient thereto, or in any way connected therewith; with power also to do a towing business, and also to purchase, own, lease, construct, control, and operate and sell docks, wharves, landings, floats, warehouses, dry docks and dock machinery, appliances and apparatus of all kinds; and with the power also to do a general shipbuilding, stevedore, dockage, warehouse, and commission business; to conduct a general cold storage and refrigeration business.

(o) To subscribe for, or cause to be subscribed for, buy, own, hold, purchase, receive, or acquire, and/or to sell, negotiate, guarantee, assign, deal in, exchange, transfer, mortgage, pledge and/or otherwise dispose of shares of the capital stock, scrip, bonds, coupons, mortgages, debentures, debenture stock, securities, notes, acceptances, drafts, and/or evidences of indebtedness issued and/or created by any government or by any political subdivision thereof or by any other corporations,

joint stock companies, or associations, whether public, private, or municipal, or any corporate body, and while the owner thereof, to possess and to exercise in respect thereof all the rights, powers, and privileges of ownership, including the right to vote thereon; to guarantee the payment of dividends on any shares of the capital stock of any of the corporations, joint stock companies, or associations in which this corporation has or may at any time have an interest, and to become surety in respect of, endorse, or otherwise guarantee the payment of the principal of or interest on any scrip, bonds, coupons, mortgages, debentures, debenture stock, securities, notes, drafts, bills of exchange, or evidences of indebtedness, issued or created by any such corporations, joint stock companies, or associations; to assume and agree to pay all or part of the indebtedness, evidenced by bonds or otherwise, of any corporation, and to assume and agree to perform any covenants, conditions, or agreements contained in any mortgage or trust indenture, and to assume any other obligation, or liability of any corporation; to become surety for or guarantee the carrying out and performance of any and all contracts, leases, and obligations of every kind of any corporations, joint stock companies, or associations, and in particular of any corporation, joint stock company, or association any of whose shares, scrip, bonds, coupons, mortgages, debentures, debenture stock, securities, notes, drafts, bills of exchange, or evidences of indebtedness, are at any time held by or for this corporation, and to do any acts or things designed to protect, preserve, improve or enhance the value of any such shares, scrip, bonds, coupons, mortgages, debentures, debenture stock, securities, notes, drafts, bills of exchange, or evidences of indebtedness, provided, however, that this Subdivision (o) shall not be construed to authorize this corporation to engage in the business of banking.

(p) To manufacture, buy, sell, and generally deal in, goods, wares, merchandise, property, and commodities of any and every class and description, and all articles used or useful in connection therewith; to engage in any business whether manufacturing or otherwise which -this corporation may deem advantageous or useful in connection with any or all of the foregoing, and to purchase, acquire, manufacture, market, or prepare for market, sell or otherwise dispose of any article, commodity, or thing which this corporation may use in connection with its business.

(q) To manage, operate, conduct and supervise the business, properties, and affairs, in whole or in part, of any companies, corporations, joint stock companies, syndicates, partnerships, and associations of all kinds whether it owns any or all of the securities and/or obligations of such companies, corporations, joint stock companies, syndicates, partnerships, and associations or not.

(r) To secure, purchase, acquire, apply for, register, own, hold, sell, or dispose of any and all copyrights, trademarks and other trade rights.

(s) To organize, or cause to be organized, under the laws of the State of Delaware, or of any other state, territory, or country, or the District of Columbia, a

corporation or corporations for the purpose of accomplishing any or all of the objects for which this corporation is organized, and to dissolve, wind up, liquidate, merge or consolidate any such corporation, or corporations, or to cause the same to be dissolved, wound up, liquidated, merged, or consolidated.

(t) To purchase, apply for, obtain, or otherwise acquire any and all letters patent, licenses, patent rights, patented processes, and similar rights granted by the United States or any other government or country, or any interest therein, or any inventions which may seem capable of being used for or in connection with any of the objects or purposes of this corporation, and to use, exercise, develop, sell, dispose of, lease, grant licenses in respect to, or other interests in the same, and otherwise turn the same to account, and to carry on any business, manufacturing or otherwise, which may be deemed to directly or indirectly aid, effectuate, or develop, the objects or any of them of this corporation.

(u) To lend money, to borrow money for any of the purposes of this corporation, and to issue bonds, debentures, debenture stock, notes, and other obligations, and to secure the same by pledge or mortgage of the whole or any part of the property, of this corporation, either real or personal, or to issue bonds, debentures, debenture stock, notes, or other obligations without any such security.

(v) To enter into, make, perform, and carry out contracts of every kind for any lawful purpose, without limit as to amount, with any person, firm, association, or corporation.

(w) In connection with its business, to draw, make, accept, endorse, discount, guarantee, execute, and issue promissory notes, bills of exchange, drafts, warrants and all kinds of obligations and certificates and negotiable or transferable instruments.

(x) To purchase, hold, sell, and transfer shares of its own capital stock, bonds, notes, and other obligations of this corporation from time to time to such extent and in such manner and upon such terms as its Board of Directors shall determine; provided that any purchase of any of the shares of the capital stock of the corporation shall not be made when such purchase would cause any impairment of the capital of the corporation; and provided further that shares of its own capital stock belonging to this corporation shall not be voted upon directly or indirectly.

(y) To have one or more offices, to carry on any or all of its operations and business and without restriction or limit as to amount, to purchase, lease, or otherwise acquire, hold, and own, and to mortgage, sell, convey, lease or otherwise dispose of, real and personal property of every class and description in any of the states or territories of the United States and in the District of Columbia, and in any and all foreign countries, subject to the laws of such state, district, territory, or country.

(z) To do any and all things herein set forth, and in addition such other acts and things as are necessary or convenient to the attainment of the purposes of this corporation, or any of them, to the same extent as natural persons lawfully might or could do in any part of the world.

The foregoing clauses shall be construed both as objects and powers and it is hereby expressly provided that the foregoing enumeration of specific power shall not be held to limit or restrict in any manner the powers of this corporation, and are in furtherance of, and in addition to, and not in limitation of the general powers conferred by the laws of the State of Delaware.

It is the intention that the purposes, objects and powers specified in this Article Third and all subdivisions thereof shall, except as otherwise expressly provided, in nowise be limited or restricted by reference to or inference from the terms of any other clause or paragraph of this Article, and that each of the purposes, objects, and powers specified in this Article Third shall be regarded as independent purposes, objects, and powers.

**FOURTH:** (a) The total number of shares of stock which this corporation shall have authority to issue is six hundred and fifty million (650,000,000) shares of which fifty million (50,000,000) shares shall be shares of Preferred Stock with a par value of one cent (\$.01) each, amounting in aggregate to five hundred thousand dollars (\$500,000), two hundred fifty million (250,000,000) shares shall be shares of Common Stock Series A of the par value of twenty-five cents (\$.25) each, amounting in the aggregate to sixty two million five hundred thousand dollars (\$62,500,000), and three fifty hundred million (350,000,000) shares shall be of common Stock Series B of the par value of twenty-five cents (\$.25) each, amounting in the aggregate to eighty-seven million five hundred thousand dollars (\$87,500,000).

(b) The Preferred Stock may be issued from time to time in one or more series, and in such amounts as may be determined by the Board of Directors. The designations, powers, preferences and relative, participating optional, conversion and other rights, and the qualifications, limitations and restrictions thereof, of the Preferred Stock of each series, which shall not be fixed by the Certificate of Incorporation, shall be such as may be fixed or altered by resolution or resolutions by the Board of Directors (authority so to do being hereby expressly granted to, and vested in, the Board of Directors) to the full extent now or hereafter permitted by the laws of Delaware.

(c) The designations, powers, preferences and relative, participating, optional, conversion and other special rights, and the qualifications, limitations and restrictions thereof, of the Common Stock Series A and the Common Stock Series B shall be as follows:

(1) Whenever full dividends have been paid or declared and funds set apart for the payment of dividends on each series of

Preferred-Stock which may be issued and outstanding, for the current dividend period and for all past dividend periods in respect of which dividends are cumulative and remain unpaid, and a cash dividend upon the Common Stock Series B shall at any time and from time to time be declared and paid, there shall at that time or at any time thereafter but within the time limits hereinafter in this paragraph set forth, be declared and paid a stock dividend or dividends on the Common Stock Series A payable in shares of Common Stock Series A, the fair value as of the respective dates of declaration (as hereinafter defined) of such stock dividend or dividends paid or payable on each share of Common Stock Series A during any calendar year to be equivalent to the cash dividend or dividends paid or payable on each share of Common Stock Series B during such calendar year pursuant to this paragraph. For the purpose of the foregoing sentence the determination of the fair value of the Common Stock Series A shall be made as of the respective dates of declaration of such dividend or dividends by the Board of Directors of the corporation in its sole discretion and such determination shall be final and conclusive. Without limiting the generality of the foregoing, the Board of Directors may, in making such determination of fair value, consider the bid and asked price of the Common Stock Series A on the business day next preceding the date of the declaration of such dividend (or if not available for such date on the next preceding date on which such quotation is available) as quoted by the National Quotation Bureau, Inc. or an organization performing functions similar thereto and such other factors as the Board of Directors may deem to be relevant, including without limitation, that the value of such stock after the record date may be reduced by the declaration of the dividend and any factors which would affect the market value of such stock dividend shares. The Board of Directors of the corporation may in its sole discretion declare a dividend or dividends on the Common Stock Series A on dates different from the date on which a cash dividend or dividends are declared on the Common Stock Series B and may fix separate record dates and/or separate payment dates different from the record dates or payment dates of the cash dividend or dividends declared on the Common Stock Series B, provided however, that the record date and the payment date of any dividend on the Common Stock Series A shall be within one year from the date of declaration thereof, and provided further that the fair value as of the respective dates of declaration (as herein defined) of all stock dividends paid on each share of Common Stock Series A during any calendar year pursuant to this Paragraph shall be equivalent to the total cash dividends paid only on each share of Common Stock Series B during such calendar year pursuant to this paragraph. This paragraph shall be applicable only where a dividend is declared on the Common Stock Series B payable only in cash and the Board of Directors does not at the same time declare a dividend in an equal amount only in cash on

the Common Stock Series A, which the Board of Directors shall have the right to do. The provisions of this paragraph are not intended to cover, or apply to, any case where a dividend is declared on the Common Stock Series B payable in stock or any other property in which event the same dividend shall be declared at the same time on the Common Stock Series A as provided in paragraph (4) of subdivision (c) of this Article FOURTH. The corporation shall not issue fractional shares in satisfaction of any stock dividend but in lieu of fractional shares it shall issue scrip certificates (exchangeable, together with other scrip certificates aggregating one or more full shares, for stock certificates representing such full share or shares of stock), for any fraction of a share of stock. The terms and form of which are to be approved by the Board of Directors of the corporation. Until the exchange thereof for certificates for full shares of stock, the holders of such scrip certificates shall not be entitled to receive dividends or to vote or to any other rights and/or privileges as stockholders of the corporation. The Board of Directors of the corporation shall, in any instance, have the full power and authority to prescribe other methods by which settlement for fractional shares shall be made, in lieu of delivering such scrip certificates for fractional shares, and may, without limiting the generality of the foregoing, make a cash settlement in respect thereof in such amount as shall be determined by the Board of Directors or provide for the combination of such fractions into a number of whole shares of stock equal to the aggregate of the fractional shares which the holders of the shares of Common Stock of the corporation would otherwise be entitled to receive and the delivery thereof to the corporation or its designee as agent for said stockholders to sell the said whole shares of stock and to pay the net proceeds of the sale to those stockholders who would otherwise have been entitled to fractional shares pro rata in accordance with their respective fractional share interests and upon such other terms as may be provided by the Board of Directors of the corporation.

(2) The Common Stock Series A, at the option of the respective holders thereof, shall be exchangeable for Common Stock Series B of the corporation, from time to time, subject to the provisions hereinafter set forth in the ratio of one (1) share of Common Stock Series B for one (1) share of Common Stock Series A (whether or not any dividend shall have been declared on the Common Stock Series A and remain unpaid but this shall not prevent a stockholder who shall exchange his shares after a record date from receiving any dividend payable to Series A stockholders of record on that date), upon surrender to the corporation or to its transfer agent of the certificates of Common Stock Series A, so to be exchanged, duly endorsed in blank for transfer; provided however that if any such shares of Common Stock Series A are surrendered for exchange on or between the date on which a cash dividend is declared

on the Common Stock Series B and the date fixed by the Board of Directors of the corporation for determining the holders of the Common Stock Series B entitled to receive such cash dividend, the said shares of Common Stock Series A shall be exchanged for shares of Common Stock Series B on and as of the business day next following the record date for determining the holders of the Common Stock Series B entitled to receive such cash dividend and until such exchange is so made any such stockholder shall be treated for all purposes as the holder of the shares of Common Stock Series A so surrendered for exchange. So long as any of the Common Stock Series A remains outstanding, there shall be reserved such number of shares of Common Stock Series B for exchange as shall be required pursuant to the provisions herein contained.

(3) The Board of Directors of the corporation shall have the right, in its solo discretion, to require all of the holders of the Common Stock Series A to exchange all of their Common Stock Series A for Common Stock Series B of the corporation in the ratio of one (1) share of Common Stock Series B for one (1) share of Common Stock Series A (whether or not any dividend shall have been declared on the Common Stock Series A and remain unpaid but this shall not prevent a stockholder who shall exchange his shares after a record date from receiving any dividend payable to Series A stockholders of record on that date). Notice of the requirement for such exchange shall be given by the corporation at least thirty days prior to the date fixed for such exchange to the holders of record of all the outstanding Common Stock Series A and an affidavit of mailing of such notice by an employee of the corporation or any employee of the transfer agent shall be conclusive evidence of the mailing of such notice. If notice of such exchange shall have been duly given as herein provided, and any holder of Common Stock Series A shall not have surrendered all his certificates of Common Stock Series A to the corporation or its transfer agent for exchange, duly endorsed in blank for transfer, then from and after the exchange date so specified in the notice, any and all rights and privileges of such holders of Common Stock Series A, as holders of Common Stock Series A, shall cease and terminate, except the right to receive shares of Common Stock Series B in exchange for his shares of Common Stock Series A as hereinabove provided, and from and after the exchange date so specified in the notice all Common Stock Series A outstanding shall be and become Common Stock Series B with the effect that each holder of the outstanding shares of Common Stock Series A shall thereupon be and become the holder of one share of Common Stock Series B for every share of Common Stock Series A then held by him.

(4) In all other respects the designations, powers, preferences and relative, participating, optional, conversion and other special rights, and the qualifications, limitations and restrictions thereof, of the Common Stock Series A and the Common Stock Series B shall be the same, and without limiting the generality of the foregoing, in the event any dividends payable in any class of stock of the corporation, or in any property, are declared upon the shares of Common Stock Series B of the corporation (which the corporation by action of its Board of Directors shall have the full power and authority to do) the same dividend shall be declared upon the Common Stock Series A of the corporation and in the event any dividends payable in any class of stock of the corporation, or in any property, (except stock dividends which are paid to equalize cash dividends as hereinabove set forth) are declared upon the shares of Common Stock Series A of the corporation, (which the corporation by action of its Board of Directors shall have the full power and authority to do) the same dividend shall be declared upon the Common Stock Series B of the corporation and in the event a cash dividend shall be declared on the shares of Common Stock Series A of the corporation (which the corporation by action of its Board of Directors shall have the full power and authority to do, whenever full dividends have been paid or declared and funds set apart for the payment of dividends on each series of Preferred Stock which may be issued and outstanding, for the current dividend period and for all past dividend periods in respect of which dividends are cumulative and remain unpaid) an equal cash dividend shall be declared on the shares of Common Stock Series B of the corporation.

(d) Unless otherwise expressly required by applicable law, each holder of Common Stock Series A and Common Stock Series B shall at every meeting of the stockholders be entitled to one vote in person or by written proxy signed by him for each share of Common Stock Series A and Common Stock Series B owned by him and shall be entitled and required to vote as part of a single class, i.e., Common Stock (without distinction as to Series A or Series B) upon all such matters as may come before the stockholders including without limitation the election of directors, which shall be decided by majority vote of the Common Stock present or represented by proxy and entitled to vote at the meeting. The stockholders of this corporation shall have no preemptive right to subscribe to any issue of shares of stock of this corporation now or hereafter made.

FIFTH: The minimum amount of capital with which it will commence business is One Thousand Dollars (\$1,000.00).

SIXTH: The name and place of residence of each of the incorporators are as follows:

<u>NAME</u>	<u>RESIDENCE</u>
L.H. HERMAN	Wilmington, Delaware
WALTER LENZ	Wilmington, Delaware
W.T. HOBSON	Wilmington, Delaware

SEVENTH: This corporation is to have perpetual existence.

EIGHTH: The private property of the stockholders shall not be subject to the payment of corporate debts to any extent whatever.

NINTH: In furtherance and not in limitation of the powers conferred by the laws of the State of Delaware, the Board of Directors is expressly authorized:

To make, alter, and repeal the by-laws subject to the power of the stockholders to change or repeal such bylaws; provided, however, that prior to the second Tuesday in March, 1937, no by-laws shall be adopted or amended by the directors so as to authorize or provide (a) for the holding of any meeting of stockholders for the election of directors at any place other than Minneapolis, Minnesota or at any time prior to the holding of the first annual meeting of stockholders for election of directors on the second Tuesday in March, 1937; or (b) for the holding of meetings of directors, prior to such first meeting of stockholders for the election of directors, at any place other than as provided in the original by-laws;

To set apart out of any of the funds of the corporation available for dividends a reserve or reserves for any proper purpose and to alter or abolish any such reserve;

To fix, determine, and vary from time to time the amount to be maintained as surplus and the amount or amounts to be set apart for working capital.

All of the powers of this corporation, insofar as the same lawfully may be vested by this Certificate in the Board of Directors, are hereby conferred upon the Board of Directors of this corporation.

Directors need not be elected by ballot, unless voting by ballot shall be requested by the holders of ten percent (10%) or more of the shares of stock represented at the meeting of stockholders at which the directors are to be elected.

TENTH: This corporation may in its by-laws make any other provisions or requirements for the management or conduct of the business of this corporation provided the same be not inconsistent with the provisions of this Certificate or contrary to the laws of the State of Delaware, and subject to the limitations upon amendment of by-laws contained in this Certificate of Incorporation.

**ELEVENTH:** This corporation reserves the right to amend, alter, change or repeal any provision contained in this Certificate of Incorporation in the manner now or hereafter prescribed by law and all rights conferred on officers, directors, and stockholders herein are granted subject to this reservation.

**TWELFTH:** A. A director of the corporation shall not be personally liable to the corporation or its stockholders for monetary damages for breach of fiduciary duty as a director, except for liability (i) for any breach of the director's duty of loyalty to the corporation or its stockholders, (ii) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law, (iii) under Section 174 of the Delaware General Corporation Law, or (iv) for any transaction from which the director derived an improper personal benefit. If the Delaware General Corporation Law is amended after approval by the stockholders of this Article to authorize corporation action further eliminating or limiting the personal liability of directors, then the liability of a director of the corporation shall be eliminated or limited to the fullest extent permitted by the Delaware General Corporation Law, as so amended.

B. No modification or repeal of the provisions of this Article shall adversely affect any right or protection of any director of the corporation existing at the date of such modification or repeal or create any liability or adversely affect any such right or protection for any acts or omissions of such director occurring prior to such modification or repeal.

IN WITNESS WHEREOF, said CITIZENS UTILITIES COMPANY has caused this Certificate to be signed by L. Russell Mitten, its Vice President, and attested by Charles J. Weiss, its Secretary, on this 17th day of June, 1996.

CITIZENS UTILITIES COMPANY

By: Livingston E. Ross  
Livingston E. Ross  
Vice President

ATTEST:

By: Charles J. Weiss  
Charles J. Weiss  
Secretary

# CITIZENS UTILITIES COMPANY

## CERTIFICATE OF SECRETARY

I, Susan M. Redner, Assistant Secretary of **CITIZENS UTILITIES COMPANY**, (the "Company"), a corporation duly organized and validly existing under the laws of the State of Delaware, do hereby certify that the following resolutions are true and correct as duly adopted by the Board of Directors of the Company as of June 29, 1999, and that such resolutions are in full force and effect, having never been revoked, amended, rescinded or annulled:

**RESOLVED**, that the Company, or its subsidiaries, acquire for \$664 million certain local telephone exchange assets from GTE Corporation and certain of its subsidiaries now constituting approximately 187,000 access lines located in the states of Arizona, California and Minnesota; and it is

**FURTHER RESOLVED**, that the action of the officers of the Company in executing on behalf of the Company, asset purchase agreements referenced in the prior resolution is hereby ratified by the Board of Directors, and it is

**FURTHER RESOLVED**, that the Company, or its subsidiaries, acquire for \$1.65 billion certain local telephone exchange assets from US WEST Communications, Inc. now constituting approximately 530,000 access lines located in the states of Arizona, Colorado, Idaho, Iowa, Minnesota, Montana, Nebraska, North Dakota and Wyoming; and it is

**FURTHER RESOLVED**, that the action of the officers of the Company in executing on behalf of the Company, asset purchase agreements referenced in the prior resolution is hereby ratified by the Board of Directors, and it is

**FURTHER RESOLVED**, that the officers of the Company are hereby authorized to make application in the name of the Company to the FERC and any state regulatory commissions asserting financing jurisdiction over the Company for approval of financing necessary or desirable to effectuate the transactions provided for in the asset purchase agreements; and it is

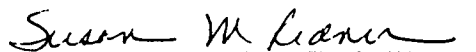
**FURTHER RESOLVED**, that the officers of the Company are hereby authorized to cause to be incorporated in the State of Delaware or in such other jurisdictions they determine to be appropriate, subsidiaries of the Company to

acquire and operate all or a portion of the assets to be acquired from GTE Corporation, and its subsidiaries, and U.S. WEST Communications, Inc.; and it is

**FURTHER RESOLVED**, that the officers of the Company are hereby authorized to make applications to the FCC and state regulatory commissions for all approvals necessary or desirable for the transfer of the local exchange assets to the Company or its subsidiaries, for the transfer of licenses, for operating authority and for all other approvals or authority deemed appropriate by the officers; and it is

**FURTHER RESOLVED**, that the officers of the Company are hereby authorized to take all actions necessary to effectuate the transactions provided for in the asset purchases.

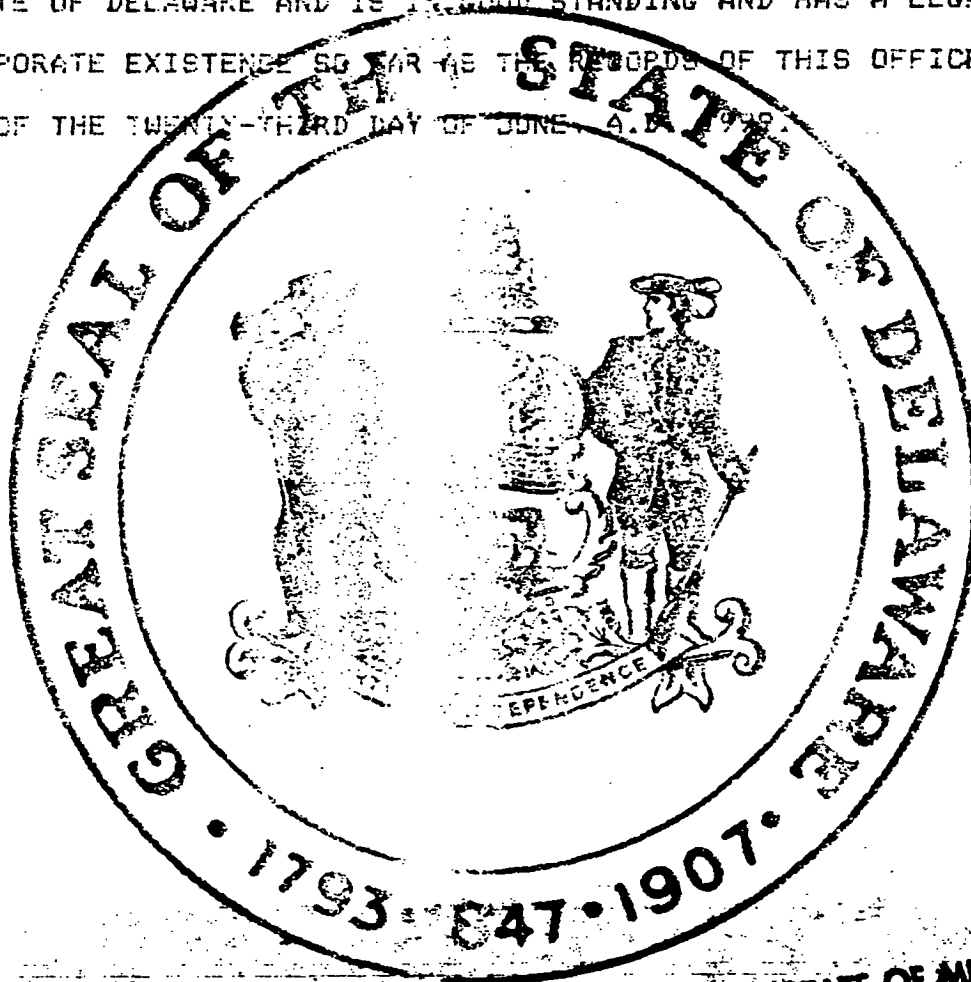
**IN WITNESS WHEREOF**, I have hereunto set my hand and caused the seal of the Company to be affixed hereto, as of the 9th day of September, 1999.

  
\_\_\_\_\_  
Susan M. Redner, Assistant Secretary

State of Delaware  
Office of the Secretary of State

097886

I, EDWARD J. FREEL, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY "CITIZENS TELECOMMUNICATIONS COMPANY OF MINNESOTA, INC." IS DULY INCORPORATED UNDER THE LAWS OF THE STATE OF DELAWARE AND IS IN GOOD STANDING AND HAS A LEGAL CORPORATE EXISTENCE SO FAR AS THE RECORDS OF THIS OFFICE SHOW AS OF THE TWENTY-THIRD DAY OF JUNE, A.D. 1999.



STATE OF MINNESOTA  
DEPARTMENT OF STATE  
FILED  
STATE TO MINN  
JUN 24 1999  
Edward J. Freel  
Secretary of State

3056413 8300  
991253725



Edward J. Freel, Secretary of State  
8B22759

AUTHENTICATION:  
DATE: 06-23-99

3

Exhibit 3

STATE OF MINNESOTA DEPARTMENT OF REVENUE

**STATE OF MINNESOTA**  
**DEPARTMENT OF STATE**

I hereby certify that this is a true and complete copy of the document as filed for record in this office.

DATED 10/25/1911

*Henry H. Lawrence*

By Wanda J. Peters

State of Minnesota

97886

## SECRETARY OF STATE

### Certificate of Authority to Transact Business

I, Mary Kiffmeyer, Secretary of State of Minnesota, do certify that: The following corporation has duly complied with the relevant provisions of Minnesota Statutes, Chapter 303, and is authorized to do business in Minnesota on and after this date with all the powers, rights and privileges, and subject to the limitations, duties and restrictions, set forth in that chapter.

Name of Corporation in Minnesota:

Citizens Telecommunications Company of Minnesota, Inc.

Name of Corporation in State of Incorporation:

Citizens Telecommunications Company of Minnesota, Inc.

Corporate Charter Number: 97886

State of Incorporation: DE

Registered Office in Minnesota:

33 S 6th Str - Multifoods Twr  
Mpls MN 55402

Name of Registered Agent: Corporation Service Company

This certificate has been issued on 06/24/1999.



*Mary Kiffmeyer*  
Secretary of State.

3 Pages

Exhibit 4



Minnesota Secretary of State

FOREIGN CORPORATION REGISTRATION TO TRANSACT BUSINESS IN MINNESOTA

097886

PLEASE TYPE OR PRINT IN BLACK INK.

FILING FEE: \$200 (\$50 if Non-Profit)

1. YOU MUST ATTACH A CERTIFICATE OF GOOD STANDING OR STATUS ISSUED BY THE FILING OFFICER IN THE STATE OR JURISDICTION IN WHICH THIS COMPANY IS DOMICILED.

2. The name of this corporation is:

Citizens Telecommunications Company of Minnesota, Inc.
Legal Name of Corporation

m

3. If the exact legal name of this corporation is unavailable in Minnesota, please complete, approve and execute the resolution at the bottom of this form and list the alternate name here:

4. The state or country under the laws of which the corporation is incorporated is: Delaware

5. The name and address of the registered agent and registered office in the State of Minnesota is:
Corporation Service Company
Full Name of Registered Agent

Registered Address: 33 South Sixth Street, Multifoods Tower, Minneapolis, MN 55402
Street address or rural route and rural route box number of the registered agent in Minnesota (cannot be a P. O. Box)

By registering the corporation irrevocably consents to service of process on it as provided by Minnesota Statutes chapter 303.13 and 5.25.

6. This corporation is a (check one) non-profit X for-profit entity.

I certify that I am authorized to execute this application and I further certify that I understand that by signing this application. I am subject to the penalties of perjury as set forth in section 609.48 as if I had signed this application under oath.

(Signature)
(President, Vice President, Secretary or Assistant Secretary)

WHEREAS, the name of this corporation is currently on file with the Secretary of State of Minnesota, and WHEREAS, the corporation has not obtained the use of this name through the consent or affidavit procedures permitted by Minnesota Statutes chapter 302A.115, THEREFORE, BE IT RESOLVED, that this corporation shall use the name

(Alternate name must also include a corporate designation) which meets all the requirements of Minnesota Statutes chapters 303.05 and 302A.115, as its name in the State of Minnesota for all purposes.

Approved on Day Month Year by the Proportion

STATE OF MINNESOTA DEPARTMENT OF STATE FILED

Vote of the JUN 24 1999

Directors of Corporate Name

(Signature) Secretary of State

Authorized Signature

I certify that this is the actual text of the approved resolution.

07930898 Rev. 11/98

019340

2

CITIZENS UTILITIES

PROCEED STEADY

1968 ANNUAL REPORT

## Our Mission

To be a world-class growth company.

As a business organization, we endeavor to provide our employees with an enriching and rewarding work experience and environment.

As a public service company, we strive to exceed the expectations of our customers and the communities we serve.

As a publicly held company, we manage the operations and growth of our resources to maximize corporate value and return for our shareholders.

## Our Values

In the pursuit of our corporate goals, we will strive to:

1. Treat one another with respect

2. Be scrupulously ethical in all of our dealings

3. Always take the initiative

4. Be an outstanding citizen in each of the communities we serve

5. Preserve and protect our environment

6. Take pride in our work and pleasure in what we do

**FINANCIAL HIGHLIGHTS** For years ended December 31,

(Dollars in millions except per-share amounts)	Citizens Communications and Public Services		Electric Lightwave, Inc. <sup>(1)</sup>		Special Items <sup>(2)</sup>		As Reported	
	1998	1997	1998	1997	1998	1997	1998	1997
Revenue	\$1,444.5	\$1,356.6	\$ 97.8	\$ 57.7	\$ —	\$ (20.7)	\$1,542.3	\$1,393.6
Operating income	264.6	244.3	(75.7)	(37.4)	(10.7)	(191.1)	178.2	15.8
EBITDA <sup>(3)</sup>	545.2	511.9	(44.6)	(26.3)	(42.6)	(116.8)	458.0	368.8
Net income	120.4	117.9	(34.7)	(23.8)	(28.6)	(84.0)	57.1	10.1
Earnings per share <sup>(4)</sup>	\$ 0.47	\$ 0.45	\$ (0.14)	\$ (0.09)	\$ (0.11)	\$ (0.32)	\$ 0.22	\$ 0.04
Weighted average shares outstanding <sup>(4)</sup>							258.9	260.2
Total assets							\$5,292.9	\$4,872.9
Customers							1,820,444	1,742,665
Employees							6,700	6,100

<sup>(1)</sup> Electric Lightwave, Inc. (ELI) is the company's 83% owned competitive access provider subsidiary. EBITDA, net income and earnings per share are presented net of the associated minority interest.

<sup>(2)</sup> For 1998, special items include the non-cash write down of the company's investment in Hungarian Telephone & Cable Corp. of \$31.9 million (\$19.7 million after tax), the cumulative effect of a change in accounting principle at ELI of \$2.3 million (net of tax), and Y2K and separation costs of \$10.7 million (\$6.6 million after tax). For 1997, special items include a pre-tax charge to earnings of \$197 million (\$135.2 million after tax) and pre-tax non-operating gain of \$78.7 million (\$51.2 million after tax) on the sale of stock by a subsidiary. See Notes to Financial Statements in the 1998 Form 10-K for a complete discussion of these items.

<sup>(3)</sup> EBITDA is earnings before interest, income taxes, depreciation and amortization.

<sup>(4)</sup> 1997 adjusted for subsequent stock dividends.

Citizens Utilities provides telecommunications and utility services, including gas, electric, water and wastewater treatment, to 1.8 million customers in 22 states.

Citizens common stock and Citizens Equity Providing Preferred Income Convertible Securities (EPPICS) are traded on the New York Stock Exchange under the symbols CZN and CZNPr, respectively.

On November 25, 1997, the common stock of Citizens' subsidiary, Electric Lightwave, Inc., began trading as a National Market Issue under the NASDAQ symbol ELIX.

Citizens Utilities' 1998 Form 10-K, filed with the Securities and Exchange Commission, has been made a part of this annual report to provide readers with an in-depth review of the company's financial and operating results.

We will make those choices that  
promise to maximize value and returns  
for our shareholders.

In 1998, Citizens Utilities continued building value through internal growth, reductions in operating expenses and the pursuit of acquisitions and joint ventures.

#### Telecommunications

During 1998, revenue from Citizens Communications' 951,500 access lines rose 2%, to nearly \$835 million, despite the shutdown of our long-distance enterprise. Citizens Communications provides its customers with an ever-increasing selection of high-quality communications services and products, such as Internet access via "Citizens Link," high-speed data transport and a wide variety of enhanced calling features.

To assure that we continue as the provider of choice in all of our markets, we are developing next-generation processes and pricing scenarios aimed at assuring customer retention by providing the highest quality of service at the most competitive prices. As part of this strategy, we have begun outsourcing many business processes that are not our core competencies. In 1998, for example, we selected AT&T to provide the nationwide network for our long-distance product. This agreement allows us to offer our local exchange customers premier long-distance services at very competitive prices.

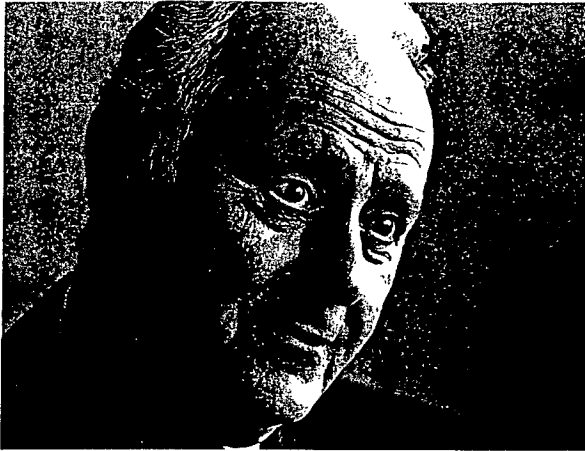
Every Citizens Communications employee is concentrating on identifying new opportunities and implementing strategies to take advantage of them. New business-oriented data services, such as frame relay, asynchronous transfer mode (ATM) and Internet access, are among the ways we are widening our business footprint and increasing margins.

Acquisitions that expand our existing markets or create new clusters, such as our 1998 acquisition of Rhinelander Telecommunications, Inc., are additional drivers of growth. Rhinelander, which provides local telephone, broadband, Internet access, paging and long-distance services to 24,000 customers in a pristine and fast-growing area of Wisconsin, is typical of the kind of properties that fit the Citizens Communications model.

#### Public Services

Revenue for Citizens Public Services, which provides gas, electric, water and wastewater treatment services, was \$610 million, up 13% over 1997. This increase reflects the addition of The Gas Company in Hawaii, acquired by Citizens in October 1997. Hawaii gas and electric services now generate approximately one-third of all revenue within the Public Services sector.

Citizens Public Services ended 1998 with over 867,000 customers. Our most significant growth opportunities are concentrated in Arizona, California, Hawaii, Illinois, Louisiana and Pennsylvania, where our largest numbers of customers are located. In these states, we have been especially successful at growing our customer base, leveraging our brands, bundling a variety of utility services to capitalize on additional opportunities for economies of scale, and consolidating our administrative network to reap greater benefits from joint marketing efforts. Many operations within Citizens Public Services have grown through acquisitions that have expanded our existing market clusters. Over the years, a number of geographically



Dr. Leonard Tow  
*Chairman and Chief Executive Officer*



Dr. Daryl A. Ferguson  
*President and Chief Operating Officer*

related acquisitions have been made in Louisiana and at our water operations in Arizona, Illinois and Pennsylvania.

In 1998, Citizens Water Resources broke ground in Arizona on its latest joint venture with the developer Del Webb. Anthem Parkside, a master-planned 5,700-acre community 20 miles north of Phoenix, will have 14,500 homes. Renewable water resources are at the heart of the environmentally friendly plan for this desert development. Rather than use Arizona's limited supplies of groundwater, Citizens built a pipeline and constructed a unique water and wastewater treatment campus with state-of-the-art technology to utilize supplies of Colorado River water from the Central Arizona Project to meet all the water needs of Anthem.

We expect continued healthy customer growth and increased sales from this sector, whose operations will remain largely insulated from active competition. This growth must be balanced against increasingly stringent and costly federal and state regulations concerning the environment and our commitment to safety and high-quality service.

#### Investment Successes

Our non-operating telecommunications investments are performing well. In January 1999, Centennial Cellular Corp. completed its \$2 billion merger with CCW Acquisition Corp. Citizens realized \$206 million from the sale of its 16% stake in Centennial for a substantial profit on our investment. Our investment in Century Communications Corp., a cable television company, also performed well. The

value of the Century stock purchased in 1992 for \$12 million grew to \$70.5 million on March 5, 1999, representing a 488% return on that investment to date.

AT&T's merger with Tele-Communications, Inc. (TCI), which will take advantage of the ability of cable television's networks to offer phone service and high-speed Internet access, will also benefit Citizens shareholders. Citizens, through a joint venture with Century Communications Corp., owns a 50% interest in four cable television systems in southern California serving over 90,000 basic subscribers. It is expected that these properties will become part of a larger strategic partnership with TCI and Century. Upon consummation, Citizens will own 5.5% of this partnership, which will serve nearly 800,000 customers in the Los Angeles basin. The value of these properties has appreciated dramatically since we made our initial investment in 1994.

#### **Electric Lightwave**

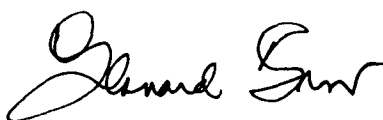
Our most important communications investment to date is Electric Lightwave, Inc. (ELI), a provider of integrated voice, video and data services in the western United States. ELI's own fiber-optic network and numerous network interconnection agreements allow it to offer high-speed data and Internet access services regionally, as well as on a national scale. ELI's 1998 revenue was \$98 million, up 69% over 1997.

ELI promises to deliver even stronger growth in operating revenue in 1999 and beyond, and we are continuing to invest in its expansion program. We are confident that ELI will meet its 1999 revenue targets

and continue its movement toward positive EBITDA. Before long, Citizens and ELI shareholders will begin to reap important benefits from its continued robust growth and profitability.

#### **1999 and Beyond**

In 1998, we announced our intention to separate Citizens into two stand-alone, publicly traded companies. While we continue to pursue separation, changing market conditions and new business opportunities may require us to consider other options, including the sale or disposition of certain company properties and the acquisition of new operations. Ultimately, we will make those choices that promise to maximize value and returns for our shareholders. This is our guiding principle.



Leonard Tow

*Chairman and Chief Executive Officer*



Daryl A. Ferguson

*President and Chief Operating Officer*

March 11, 1999

## REVIEW OF OPERATIONS

Citizens' telecommunications and utility operations, located in some of the country's most attractive high-growth markets, provide solid value for shareholders, customers and employees. Our strategy is to capitalize upon every opportunity our industries offer.

O. Lee Jobe, President of Citizens Communications, oversees an organization generating more than \$835 million in revenue and supporting 951,500 customers with a workforce of 3,600 employees.

Lee joined Citizens in 1997 as Vice President of Network Operations. He came to Citizens from Pacific Bell where he served as Vice President, Business Operations. In that role, he was responsible for all Pacific Bell business and wholesale customers. Prior to that, Lee, as Vice President of Reengineering, was responsible for managing the implementation of approximately \$900 million of reengineering initiatives and establishing Pacific Bell's operations research group.

Prior to Pacific Bell, Lee worked for Sprint Corp. as its Director, Business Operations, responsible for all private line, switched data, ISDN and video operations. He also worked at General Motors in a variety of management positions.

Lee has taught operations analysis at the Keller Graduate School of Management. He earned a Bachelor of Arts degree and a Master's degree in economics from the University of Missouri, Kansas City.

Citizens Communications is dedicated to bringing the Information Age to America's communities. This is what we call our strategic intent. We have a tremendous opportunity to grow by delivering a suite of communications services to our customers in suburban and rural America to help them better manage their professional and personal lives. Our franchised service areas enjoy attractive growth rates from a relatively stable base of customers.

Everyone benefits if Americans continue to demand high-speed, high-quality communications. That's why I want our residential customers in communities like Cookeville, Tennessee to have high-speed data services to access and to navigate the Internet, as well as a full complement of calling services such as voice mail, Caller ID and call blocking. I want to enable the students, teachers and parents in the schools we serve from Elk Grove, California to Johnstown, New York to enjoy the benefits of distance-learning applications that will give them access to the best educators in the world.

To achieve our strategic intent, we must capitalize on what we already do well, while building new competencies. Toward this end, we took important steps in the past year. We identified the top needs in our key markets and are working to address them. We are changing our processes to make them more competitive. We continue to look at acquisition opportunities that would allow us to aggressively grow the value we can bring to communities and to our shareholders. We are especially interested in acquiring properties that would help make Citizens Communications a true one-stop shop where customers can buy local, long-distance, cellular, paging, Internet access and personal communications services.

Today, Regional Bell operating companies (RBOCs) and others are going all out to defend their major metropolitan markets, which hampers their ability to invest as aggressively as they otherwise might in America's smaller communities. This year will provide us with a number of opportunities to acquire new operations in certain of these communities. While RBOCs are busy

protecting high-density population areas and high-profile business clients, we're building competencies to deliver high-value services to customers throughout our territories. We are ready to invest more capital dollars per access line in our existing and newly acquired properties than an RBOC or a GTE might; an ideal situa-



tion for customers when Citizens Communications is providing services in their community, and an ideal strategy to meet competitive challenges head on.

Our objectives are to sell multiple lines of products to our customers and to provide top-notch service. That's just good business. Customers who purchase multiple-line products and appreciate the quality of the service they receive are less likely to switch to a competitor. If anything, they will want to buy still more products. To that end, building next-generation processes

and pricing structures and developing marketing capabilities and new service offerings should assure customer retention and growth and will further improve our asset-management skills.

Data transport is one market we are targeting aggressively. We're deploying a multi-service platform, allowing us to offer high-speed data services such as frame relay, ATM or xDSL

(digital subscriber line). The xDSL product, which sends broadband traffic over ordinary telephone wires, can transmit data at speeds more than

**Our goals are straightforward. We're here to provide a wide variety of quality services to our customers so that we make money for our company and shareholders.**

10 times faster than ISDN (integrated services digital network).

This product represents a significant upgrade for customers who currently have or want ISDN, and we believe we can offer it at a very competitive price. In Elk Grove, Cookeville and other communities, we are and will be conducting xDSL trials. This technology is superior to ISDN and far superior to slower dial-up

modems. Market trials such as these allow us to better gauge public interest and test serviceability and reliability. Once we determine a



cost structure and an estimated market penetration for a community, we can develop a market plan to roll out the product to similar properties. Not every property will

receive all of these data services near term, but most will and we will deploy them aggressively.

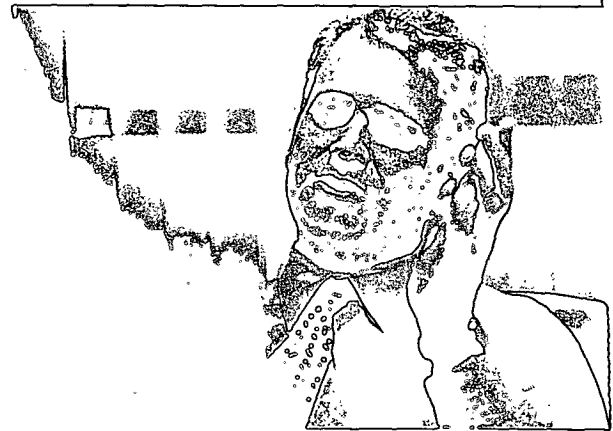
To meet our goals, it is important to realize that every Citizens Communications employee has a job to do; my job is to help each of them succeed. This means communicating the end point where I want employees to be, ensuring that they're moving efficiently in that direction, and asking the right questions to help them stay on track.

Our goals are straightforward. We're here to provide a wide variety of quality services to our customers so that we make money for our company and shareholders. I want to ensure that we both make

an appropriate rate of return on our invested capital and foster an environment that employees want to be part of.

We are focused on generating cash. Someone once told me,

“Earnings are opinion, cash is fact.” Here are the facts: Citizens Communications contributed a significant increase in free cash flow to Citizens Utilities in 1998 compared with 1997, from \$52 million to more than



\$145 million. This resulted, in part, from creating a culture that asks



tough questions before we make new investments. A new sector executive committee scrutinizes each significant capital investment and expense request. Each significant investment and expense must

have a proven business case before we approve it.

More than \$835 million of the company's 1998 revenue was generated by Citizens Communications. We are excited about our



prospects. We are growth-oriented and I think that Citizens Communications' rapidly increasing free cash flow contri-

bution will help people understand that we are a management team that uses a cash-flow focus to drive decisions.

Bringing fast and easy electronic commerce and high-quality communications to mainstream America requires the personal effort and commitment of everyone at Citizens Communications. The opportunity to grow our company by delivering unsurpassed value and superior services to our customers is compelling and we all want to be part of it.

A handwritten signature in black ink, appearing to read 'O. Lee Jobe'. The signature is stylized and fluid, with a long horizontal stroke extending to the right.

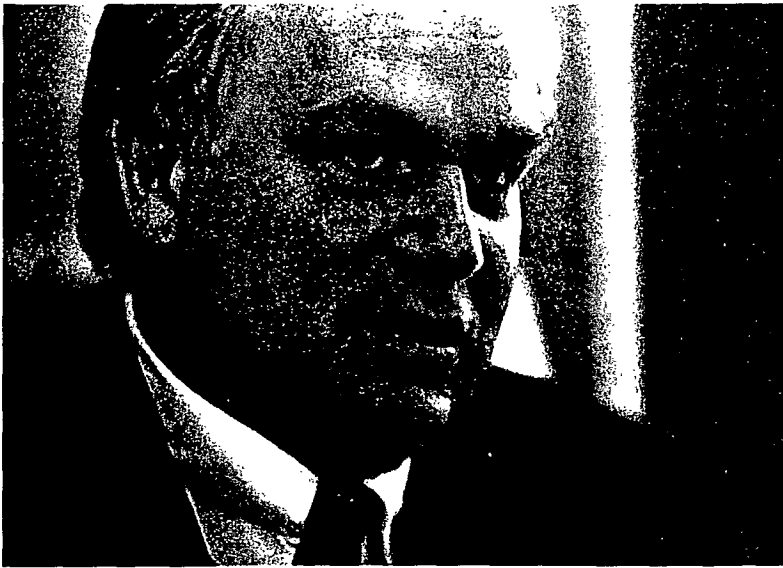
O. Lee Jobe  
*President, Citizens Communications*

J. Michael Love is President of Citizens Public Services, responsible for all aspects of the gas, electric, water and wastewater treatment operations within the sector. These operations generated \$610 million in revenue in 1998, serve 867,300 customers and have 1,800 employees.

Michael has headed Citizens Public Services since 1997. Before that, he was Vice President, Corporate Planning, responsible for strategic planning, budgets, mergers and acquisitions at Citizens. From 1984 to 1988, he was Assistant to the President and Assistant Vice President. In 1988, Michael left the company to become President and General Counsel of Southern New Hampshire Water Company, rejoining Citizens in 1990. Prior to 1984, he was a regulatory attorney with AT&T and, before that, Chairman of the New Hampshire Public Utilities Commission, during which time he was President of the New England Conference of Regulatory Commissioners.

Michael earned a Bachelor's degree from the University of Michigan and a law degree from the University of Detroit. He has lectured on regulatory matters at Dartmouth's Amos Tuck Business School, the University of New Hampshire and Franklin Pierce Law School. He is a member of the American and New Hampshire Bar Associations and the National Association of Regulatory Commissioners Emeritus.

We are at an exciting crossroads in the nearly 70-year history of Citizens Utilities. Citizens' public utility businesses have grown severalfold in the past decade. We are focused on providing increasing value to shareholders through strategic resource management and acquisition.



Today, Citizens Public Services is a \$610 million sector serving 867,300 customers in 10 states. Our primary focus is on the six states — Arizona, California, Hawaii, Illinois,

Louisiana and Pennsylvania — where we have our largest customer base, our largest employee base and our greatest potential for adding value for shareholders. We currently also operate in Colorado, Indiana, Ohio and Vermont, where we are working to grow our properties through acquisition and additional investment.

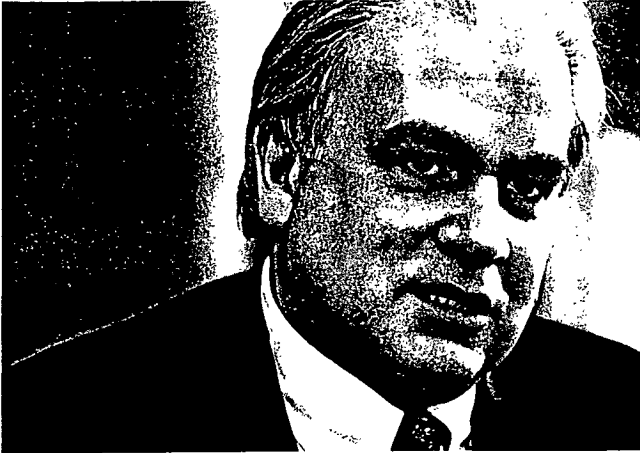
Citizens Public

Services has been energized by timely acquisitions, particularly in the gas and water businesses. These acquisitions

**Each day we have only two tasks: The first is to provide safe, reliable, quality service to our customers. And the second is to provide increasing value to our shareholders.**

have brought new ideas, vitality, creativity and talents into the Public Services sector that are worth their weight in gold. We know that we do not have a monopoly on the best ideas. And we are smart enough to learn from our new colleagues and our new customers and to put that knowledge into practice.

Size does, indeed, matter. But it's not only the number of customers we have and the number of dollars of revenue; it's also the level at which we can increase value for our shareholders. That's going to necessitate expanding some of our existing operations beyond their current size and disposing of other assets that are not sufficiently productive.



Arizona is fast becoming the model for the success of our new strategy. We have an excellent opportunity to increase gas revenue and profits in the state. We have lower rates than competing

energy providers, a well-trained work force and a presence in key areas of the state that are growing rapidly. In the water/wastewater arena, we are working with premier developers such as Del Webb to establish new properties near or adjacent to our existing operations. And our Pennsylvania operations are experiencing dramatic growth and have been leaders in our efforts to focus on safety and quality.

In Hawaii, too, we have tremendous upside as the largest gas provider in the islands and as a significant electric provider. I see Hawaii continuing to be a major force within Citizens for delivering increasing value to our shareholders.



Louisiana Gas Service is Citizens Public Services' biggest operation. By adding a number of smaller natural gas companies in adjacent markets, we have continued to improve our

economies of scale there. We have a very capable work force that is willing to take innovative risks, such as partnering with larger companies, allowing us to jointly serve customers we would not have been able to serve before.

Our utility businesses will always be regulated in some fashion. That's not going to go



away. But we will have to compete against new entities that are not regulated. As a consequence, we have to be quicker and more innovative in finding value. We are adopting the mind-set of non-regulated companies. The management team we've put together knows its competition and is driving our business to maximize shareholder value by lowering operating costs. We're developing and aggres-

sively marketing new products and services rather than simply looking to the regulatory arena for rate relief. We've made significant strides in reducing our overhead costs by consolidating support services. As a consequence, we are able to price our products and services more competitively. I think we are ahead of our peers on the learning curve in reducing costs. Our productivity is steadily increasing, the efficiency of our deployment of capital has vastly improved and we're rigorously searching for new earnings opportunities.

My objective is to make sure that the Citizens Public Services staff is aware of the need to bring increasing value to shareholders every day. Each day we have only two tasks: The first is to provide safe, reliable, quality service to our customers. And the second is to provide increasing value to our shareholders.

A handwritten signature in cursive script that reads "J. Michael Love". The signature is written in black ink and is positioned above the printed name and title.

J. Michael Love

*President, Citizens Public Services*

**CITIZENS UTILITIES COMPANY**

**FORM**

UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 1998

Commission file number 001-11001

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934

**CITIZENS UTILITIES COMPANY**

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of  
incorporation or organization)

06-0619596

(I.R.S. Employer Identification No.)

3 High Ridge Park

P.O. Box 3801

Stamford, Connecticut 06905

(Address, zip code of principal executive offices)

Registrant's telephone number, including area code: (203) 614-5600

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

Common Stock, par value \$.25 per share

Guarantee of Convertible Preferred Securities of Citizens Utilities Trust

Citizens Convertible Debentures

Guarantee of Partnership Preferred Securities of Citizens Utilities Capital L.P.

(Title of each class)

New York Stock Exchange

New York Stock Exchange

N/A

N/A

(Name of exchange on which registered)

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

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of 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 10-K. [ ]

The aggregate market value of the voting stock held by nonaffiliates of the registrant as of February 26, 1999 was \$1,935,322,722.

The number of shares outstanding of the registrant's Common Stock as of February 26, 1999 was 259,884,972.

DOCUMENTS INCORPORATED BY REFERENCE

The Proxy Statement for the registrant's 1999 Annual Meeting of Stockholders to be held on May 20, 1999, is incorporated by reference into Part III of this Form 10-K.

## Table of Contents

	<u>Page</u>
<b>Part I</b>	
Item 1.	3
Description of Business .....	3
General Development of Business .....	3
Financial Information about Industry Segments .....	3
Narrative Description of Business .....	3
Communications .....	3
CLEC .....	7
Public Services .....	8
Gas .....	8
Electric .....	9
Water and Wastewater .....	11
General .....	12
Financial Information about Foreign and Domestic Operations and Export Sales .....	13
Item 2.	13
Description of Property .....	13
Item 3.	14
Legal Proceedings .....	14
Item 4.	15
Submission of Matters to Vote of Security Holders .....	15
Executive Officers .....	15
<b>Part II</b>	
Item 5.	16
Market for the Registrant's Common Equity and Related Stockholder Matters ..	16
Item 6.	17
Selected Financial Data .....	17
Item 7.	18
Management's Discussion and Analysis of Financial Condition and Results of Operations .....	18
Item 7A.	31
Quantitative and Qualitative Disclosures About Market Risk .....	31
Item 8.	31
Financial Statements and Supplementary Data .....	31
Item 9.	31
Changes in and Disagreements with Accountants on Accounting and Financial Disclosure .....	31
<b>Part III</b>	31
Incorporation by Reference to the 1999 Proxy Statement .....	31
<b>Part IV</b>	
Item 14.	31
Exhibits, Financial Statement Schedules and Reports on Form 8-K .....	31
Signatures .....	35
Index to Consolidated Financial Statements .....	F-1

## **Part I**

### **Item 1. Description of Business**

This annual report on Form 10-K contains forward-looking statements that are subject to risks and uncertainties which could cause actual results to differ materially from those expressed or implied in the statements. Further discussion regarding forward-looking statements, including the factors which may cause actual results to differ from such statements, is located in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations," in this report.

#### **(a) General Development of Business**

The "Company" includes Citizens Utilities Company and its subsidiaries except where the context or statement indicates otherwise. The Company provides, either directly or through subsidiaries, communications services, competitive local exchange carrier (CLEC) services and public services including gas transmission and distribution, electric transmission and distribution, water distribution and wastewater treatment services to primarily rural and suburban customers throughout the United States.

The Company was incorporated in Delaware in 1935 to acquire the assets and business of a predecessor corporation. Since then, the Company has grown as a result of investment in owned communications and public services operations and from numerous acquisitions of additional communications, CLEC and public services operations. It continues to expand through internal investment, acquisitions and joint ventures in the rapidly evolving telecommunications industry and in traditional public services and related fields. The Company's financial resources and operating performance enable it to make the investments and conduct the operations necessary to serve growing areas and to expand through acquisitions.

On May 18, 1998, the Company announced its plans to separate its telecommunications businesses and public services businesses into two stand-alone publicly-traded companies. The Company intends to establish and transfer to a new company (Newco) all of its telecommunications businesses, including its approximate 83% interest in Electric Lightwave, Inc. (ELI). This separation is subject to federal and state regulatory approvals and final Board approval, and is expected to be carried out through a distribution in the stock of the new company to the Company's shareholders. The public services businesses will continue to operate as Citizens Utilities Company and intend to provide gas transmission and distribution, electric transmission and distribution, water distribution and wastewater treatment services. This separation is being made in recognition of the different investment features, performance criteria, capital structures, dividend policies, customers' requirements and regulatory designs of each business, and would allow each business to pursue its own strategy and compete more effectively in its respective markets. The separation is expected to strengthen both businesses and enable each of them to take full advantage of opportunities to enhance value.

The Company received an order from the Federal Energy Regulatory Commission that granted an approval necessary to proceed with its separation plans. The Company filed a request with the Internal Revenue Service for a private letter ruling that the transaction is not subject to federal income tax. The Company has filed petitions with numerous state regulatory agencies for the approvals necessary to proceed with its separation plans and to date has received the necessary approval from four of these agencies. An application with the Federal Communications Commission (FCC) for the transfer of certain licenses and filings with the Securities and Exchange Commission will also be made during the separation process. The transaction is expected to be completed in the second half of 1999.

Although the Company continues to aggressively pursue its separation plans, changing market conditions and new business opportunities may require it to consider other methods to enhance shareholder value, including the sale or other disposition of certain properties and the acquisition of new properties.

#### **(b) Financial Information about Industry Segments**

Note 14 of the Notes to Consolidated Financial Statements included herein sets forth financial information about industry segments of the Company for the last three fiscal years.

#### **(c) Narrative Description of Business**

##### **Communications**

Through subsidiaries, the Company provides both regulated and competitive communications services to residential, business and wholesale customers. Communications services consist of local network services, network access services, long distance services, directory advertising, centrex, cellular, voice mail and cable television services.

The Company operates as an Incumbent Local Exchange Carrier (ILEC) that provides local and intraLATA services to the following approximate number of retail access lines in the following states:

<u>State</u>	<u>Local Network Access Lines</u>
New York	320,900
West Virginia	143,400
Arizona	141,900
California	127,200
Tennessee	96,100
Nevada	25,800
Wisconsin	24,200
Utah	21,900
Idaho	20,600
Oregon	14,200
Montana	8,500
New Mexico	5,400
Pennsylvania	1,400
Total	<u>951,500</u>

The Company provides network access services and billing and collections services primarily to AT&T Corp., MCI Worldcom Corp. and Sprint Corp. The Company is also enhancing its network support systems to offer local resale capabilities in its local exchange franchise serving areas to emerging CLECs.

#### *Communications Strategy*

In 1998, the Company initiated a strategy designed to foster growth within its local service areas. This strategy focuses on the provision of traditional local and long distance telecommunications services while addressing emerging opportunities in the communications marketplace, such as internet and high-speed data services. The Company's goal is to strengthen its position as a full service communications provider to customers within its local service areas through the provision of an integrated package of products and services. The Company is committed to continuous improvements in operational efficiencies through the application of value based management techniques designed to aggressively generate free cash flow.

The Company continues to look at acquisition opportunities. The Company is especially interested in acquiring properties that would help make its Communications business a full service provider from which customers can buy local, long distance, cellular, paging, Internet access and personal communications services.

#### *Telecommunications Act*

In February 1996, the Telecommunications Act of 1996 (the 1996 Act) became law. The national public policy framework for telecommunications was changed dramatically by the 1996 Act. A central focus of this sweeping policy reform was to open local telecommunications markets to practical competition. The 1996 Act preempts state and local laws to the extent that they prevent competitive entry into the provision of any telecommunications service. Under the 1996 Act, however, states retain authority to impose on carriers requirements necessary to preserve universal telecommunications service, protect public safety and welfare, ensure quality of service and protect consumers. States are also responsible for mediating and arbitrating interconnection agreements between CLECs and ILECs if voluntary negotiations fail.

Pursuant to the requirements of the 1996 Act, the FCC has been and will be conducting rule-making proceedings resulting in a number of new rules that could impact the operations of the Company. These rules, described in more detail below, address interconnection, universal service reform and access charge/price cap reform.

#### *Interconnection*

The FCC's Interconnection Order, issued in August 1996, addresses the relationship between ILECs, such as the Company, and CLECs, such as the Company's subsidiary, ELI.

The 1996 Act and the Interconnection Order outline three routes, which are not mutually exclusive, to competitive market entry. The first is through a CLEC's construction and operation of its own local exchange facilities, in which case the sole requirement of the ILEC is interconnection for purposes of traffic interchange. The second allows a CLEC to acquire, at incremental cost, unbundled network elements from the ILEC for CLEC assembly into

end-to-end local exchange services and/or as a supplement to the facilities it has constructed on its own. The third is through CLEC resale of ILEC retail services acquired from the ILEC at wholesale rates.

Subject to the rural telephone company exemption discussed below, the Interconnection Order affects the Company's local network services business as follows:

- (a) ILECs must provide interconnection to telecommunications carriers at any technically feasible point, equal in quality to that provided for the ILECs' own operations;
- (b) ILECs must provide those carriers with access to network elements on an unbundled basis;
- (c) ILECs must offer for resale, at wholesale rates, any telecommunications services that the ILECs provide at retail to subscribers who are not telecommunications carriers;
- (d) ILECs and CLECs must compensate each other for the termination of interchanged local exchange traffic.

All of the provisions of the Interconnection Order could materially impact the Company's financial position and results of operations. Because of its smaller size and smaller market service areas, the Company's local network services business has a qualified exemption from the FCC's Interconnection Order. The qualified exemption pertains to certain technical requirements imposed upon ILECs and is neither an exemption from interconnection, in general, nor against competitive entry by other carriers. This exemption is known as the rural telephone company exemption and it continues until a bonafide request for interconnection is received and a state commission with jurisdiction determines that discontinuation of the exemption is warranted, consistent with universal service principles, and that such discontinuation will not impose an undue economic hardship on the Company and the interconnection requested is technically feasible. The Company has received over 100 interconnection requests from CLECs and wireless communications providers. With respect to CLEC interconnection, three contracts have been approved by state commissions. The Company will be providing unbundled network elements in 1999. The Company has signed resale contracts in Arizona, Nevada and New York and continues to receive additional requests for resale. None of Citizens' bonafide requests for interconnection received and finalized in 1998 required payment of usage based reciprocal compensation to CLECs. Reciprocal compensation is payment for the transport and termination of local traffic between the Company and a network-based CLEC. The first contract with a CLEC for usage based reciprocal compensation will begin in 1999. On February 25, 1999, the FCC issued a Declaratory Ruling and Notice of Proposed Rulemaking that categorized calls terminated to Internet Service Providers (ISPs) as "largely" interstate in nature, which could have the effect of precluding these calls from reciprocal compensation charges. However, the ruling stated that ILECs are bound by the existing interconnection agreements and the state decisions that have defined them.

#### *Universal Service Reform*

In May 1997, the FCC released its order creating a new federal universal service system (the Universal Service Order). The Universal Service Order was the FCC's response to one of the 1996 Act's mandates for a new system for funding of ubiquitous basic exchange telephone services to all areas of the United States and its possessions through explicit contributions of all telecommunications carriers. This new system for funding of basic services in rural, high cost and insular locations is designed to end the long standing system of funding through implicit subsidies levied by ILECs in the form of artificially high, mandated prices for access, intraLATA toll, and other non-basic services. A second significant mandate of the 1996 Act addressed in the Universal Service Order is the creation of a federal funding mechanism for the provision of discounted basic and advanced telecommunications services to qualifying public primary and secondary schools and local libraries. A third mandate creates a mechanism for providing federal funding of advanced services to rural health care providers sufficient in scope to allow qualified entities to receive such services at rates comparable to those paid by health care providers in urban areas.

The Universal Service Order has implications for the Company in addressing universal service funding to rural telephone companies. First, the Company expects to continue receiving funding under the new federal universal service system. Second, the FCC determined that it is not appropriate at this time to bring rural telephone companies under a proxy-model driven universal service cost determination system in the same time frame applicable to non-rural carriers. The Company expects that its ILECs will continue receiving federal universal service funding, with certain adjustments, based upon its actual costs incurred to provide universal services for several years.

The Company cannot predict what the levels or methods of contributions will be or whether the amount of receipts from the new system will be equal to or greater than its contributions, because the new system is still under development by the FCC.

#### *Access Charge/Price Cap Reform*

In May 1997, the FCC released separate orders in its Access Reform and Price Cap Reform proceedings (the Access Reform Order and the Price Cap Reform Order, respectively). Both orders affect the Company's ILECs as the Company elected price cap regulation commencing July 1, 1996.

Price cap regulation is a form of rate regulation in which the interstate rates of affected ILECs are subject to maximums that are periodically adjusted according to formulae contained in the FCC's Rules. Price cap regulation allows affected carriers to retain all earnings generated by operating at the capped rates. In this manner, affected ILECs are rewarded for achieving operating efficiencies.

In the Access Reform Order, the FCC ordered price cap carriers to restructure certain components of the mandated interstate access structure in order to bring pricing more in line with underlying costs. The Company has complied with this FCC order since July 1, 1997, as required.

In the Price Cap Reform Order, the FCC arrived at a new productivity factor, known as the X-factor, by which ILEC price caps are lowered each year. The purpose of the X-factor adjustment is to reflect the FCC's findings that ILECs enjoy productivity gains that are proportionately greater than those experienced in other industries. The X-factor adjustment is designed to give price cap ILECs' interexchange carrier customers some of the benefits of technology-driven declining costs in local exchange telephony. The new X-factor prescribed by the Price Cap Reform Order, 6.5%, which is adjusted for inflation, is based upon data unique to the Regional Bell Operating Companies (RBOCs), with no consideration given to any other price cap regulated carriers. In particular, the Company believes that the 6.5% X-factor, which was effective July 1, 1997, is inappropriate as applied to small price cap regulated ILECs. The Company, in conjunction with the Independent Telephone and Telecommunications Alliance, is pursuing an appeal in the U. S. Court of Appeals for the District of Columbia of the 6.5% X-factor as applied to rural price cap ILECs. The appeal contends that such carriers lack the economics of scope and scale required to achieve that level of productivity growth each year. The court has not yet ruled on this appeal. The FCC will likely revisit the X-factor issue in 1999.

#### *Joint Ventures, Acquisitions and Investments*

The Company owns a one-third interest and is general managing partner of Mohave Cellular, a cellular limited partnership operating eight cell sites in Arizona.

In March 1999, Adelphia Communications Corporation (Adelphia) and Century Communications Corp. (Century) announced the signing of a definitive agreement for the merger of Century with Adelphia. The Company currently owns 1,807,095 shares of Century Class A Common Stock. Pursuant to the Merger Agreement, each Century Class A Common share will be exchanged for cash of \$9.16 and .6122 of a share of Adelphia Class A Common Stock (for a total market value of \$44.14 per Century Class A Common share based on Adelphia's March 4, 1999 closing price of \$57½).

A subsidiary of the Company, in a joint venture with a subsidiary of Century Communications Corp., acquired and operates four cable television systems in southern California serving over 90,000 basic subscribers. Century is a cable television company of which Leonard Tow, the Chairman and Chief Executive Officer of the Company, is Chairman and Chief Executive Officer. In addition, Claire Tow, a Director of the Company, is a Senior Vice President and a Director of Century. A management board on which the Company and Century are equally represented governs the joint venture. A subsidiary of Century (the Manager) manages the day-to-day operations of the systems. The Manager does not receive a management fee but is reimbursed only for the actual costs it incurs on behalf of the joint venture. The Manager is obligated to pass through to the joint venture any discount, up to 5%, off the published prices of services or assets purchased for the joint venture for use in the systems. The Manager is entitled to retain any discount in excess of 5%. The Company accounts for the joint venture following the equity method of accounting. It is expected that these properties will become part of a larger partnership with Tele-Communications, Inc., a cable operator in California, and Century. Upon formation of the partnership, the Company will own 5.5% of this partnership, which will serve approximately 772,000 customers in the Los Angeles basin. Upon consummation of the Adelphia/Century merger, the Company expects to sell to Adelphia its interest in the joint venture properties (or its interest in the partnership if the joint venture properties are transferred to the partnership before the Adelphia/Century merger).

In November 1998, the Company acquired all the stock of Rhinelander Telecommunication, Inc. (RTI) for approximately \$84 million in cash. RTI is a diversified telecommunications company engaged in providing local exchange, long distance, Internet access, wireless and cable television services to rural markets in Wisconsin.

In January 1998, the Company purchased approximately 1.3 million shares of D&E Communications (D&E) for approximately \$27 million in cash. As of December 31, 1998, this investment represented 17.9% of D&E's outstanding common stock. D&E is a full-service telecommunications company in Lancaster County, Pennsylvania that offers both local and long distance service, wireless service, Internet service, paging, voice, data and video communications equipment and computer networking services.

#### CLEC

The Company's CLEC subsidiary, ELI, is a facilities-based integrated communications provider providing a broad range of communications services. ELI provides the full range of its products and services, including switched local and long distance voice service as well as enhanced data communications services and dedicated point-to-point services, in the western United States. Enhanced data services are also offered in selected cities throughout the country. ELI markets to retail customers, who are primarily large- and medium-sized communications-intensive businesses, and to wholesale customers, who are primarily other communications providers. ELI was incorporated in 1990 and is approximately 83% owned by the Company. ELI completed the initial public offering of its common stock in November 1997.

ELI initially operated as a Competitive Access Provider (CAP) in selected western United States cities, providing point-to-point connectivity for inter-exchange carriers (IXC) and businesses. With the passage of the 1996 Act, the increase in customer demand for enhanced broadband data services and the development of competitive public data and voice networks, ELI has substantially expanded the breadth of its product offering and its geographic reach.

During 1998, ELI expanded the number of its Metropolitan Area Networks (MANs), where it provides the full range of its services on its own fiber optic network, from 5 to 7. ELI also added 2 voice switches, 3 frame relay switches, 6 Asynchronous Transfer Mode (ATM) switches and 7 Internet routers to its facilities during the year. ELI's ATM network backbone began operation in 1998 and is used to transfer voice, video images and data. Management believes the ATM network will position ELI to offer one network for all data, voice and video transmission needs. ELI's local and long-haul installed fiber optic network was expanded by 24% to 3,091 route miles during the year, and construction has started on over 2,900 route miles of additional fiber with completion scheduled for the second half of 1999. In the second half of 1998, ELI began the expansion of its enhanced data services to cities outside of its MAN network, with additional cities scheduled for addition in 1999.

The following table represents certain operating information relating to ELI:

	<u>1998</u>	<u>1997</u>
Route miles	3,091	2,494
Fiber miles	181,368	140,812
Buildings connected	766	610
Access line equivalents	74,924	34,328
Switches installed:		
Voice	7	5
Frame relay	23	20
Internet	24	17
ATM	14	8
Customers	1,644	1,165

In each of its facilities-based markets, ELI faces significant competition from the ILECs, which currently dominate the local exchange market and are a de facto monopoly provider of local switched voice services. ELI's primary ILEC competitors are US WEST, PacBell and GTE. Under certain circumstances, FCC and state regulatory authorities may provide ILECs with increased flexibility to reprice their services as competition develops and as ILECs allow competitors to interconnect to their networks. If the ILECs and other competitors lower their rates and can sustain significantly lower prices over time, this may adversely affect revenues of ELI if it is required by market pressure to price at or below the ILECs' prices. If regulatory decisions permit the ILECs to charge CAPs/CLECs substantial fees for interconnection to the ILECs' networks or afford ILECs other regulatory relief, such decisions could also have a material adverse effect on ELI.

ELI's facility-based operational CLEC competitors in the markets in which ELI operates include, among others: AT&T Local Services, GST Telecommunications, MCI WorldCom Corp. and NEXTLINK Communications. In each of the markets in which ELI operates, at least one other CLEC, and in some cases several other CLECs, offer many of the same local communications services provided by ELI, generally at similar prices.

Potential and actual new market entrants in the local communications services business include RBOCs entering new geographic markets, IXCs, cable television companies, electric utilities, international carriers, satellite carriers, teleports, microwave carriers, wireless telephone system operators and private networks built by large end users, many of which may have financial, personnel and other resources substantially greater than those of ELI. In addition, the current trend of business combinations and alliances in the communications industry, including mergers between RBOCs, may increase competition for ELI. With the passage of the 1996 Act and the entry of RBOCs into the long distance market, ELI believes that IXCs may be motivated to construct their own local facilities or otherwise acquire the right to use local facilities and/or resell the local services of ELI's competitors.

### **Public Services**

The public services sector strategy is focussed on strategically managing resources and on growth through acquisition. The Company is increasing productivity by capitalizing on economies of scale, where appropriate, disposing of non-productive assets, managing the deployment of capital, and reducing operating costs.

#### *Gas*

Operating divisions of the Company provide natural gas transmission and distribution services to the following approximate number of primarily residential customers in the following states:

<u>State</u>	<u>Customers</u>
Louisiana	274,200
Arizona	103,600
Hawaii	66,000
Colorado	13,400
Total	<u>457,200</u>

The provision of services and/or rates charged are subject to the jurisdiction of federal and state regulatory agencies. The Company purchases all needed gas supply (except for the production by the Company of synthetic natural gas in Hawaii), which is believed to be adequate to meet current demands and to provide for additional sales to new customers. The gas industry is subject to seasonal demand (except in Hawaii), with the peak demand occurring during the heating season of November 1 through March 31. The Company's gas sector experiences third party competition from fuel oil, propane and other gas suppliers for most of its large consumption customers (of which there are few) and from electric suppliers for all of its customer base. The competitive position of gas at any given time depends primarily on the relative prices of gas and these other energy sources.

In November 1998, a class action lawsuit was filed in state District Court for Jefferson Parish, Louisiana, against the Company and three of its subsidiaries: LGS Natural Gas Company, LGS Intrastate, Inc. and Louisiana General Service Company. The lawsuit alleges that the Company and the other named defendants passed through in rates charged to Louisiana customers certain costs that plaintiffs contend were unlawful. The lawsuit seeks compensatory damages in the amount of the alleged overcharges and punitive damages equal to three times the amount of any compensatory damages, as allowed under Louisiana law. In addition, the Louisiana Public Service Commission has indicated its intention to open an investigation into the allegations raised in the lawsuit. The Company and its subsidiaries believe that the allegations made in the lawsuit are unfounded and the Company will vigorously defend its interests in both the lawsuit and the related Commission investigation.

The Company seeks to expand into high growth areas adjacent to its Louisiana operations. The Company targeted the high growth areas of the River Parishes and Northlake districts. In October 1998, the Company acquired St. Charles Natural Gas Company for \$5,000,000 in cash. St. Charles Natural Gas Company is a natural gas distribution company serving 5,000 customers in Louisiana and will become part of the Company's Louisiana Gas Services operations. This acquisition will provide expansion opportunities in the St. Charles, Lafourche, Ascension and Iberville Parishes. In July 1998, the Company began managing the operations of the Pine Pipeline in north Louisiana and contracted with a new industrial customer for a ten-year supply contract.

The Company continues to expand its Arizona gas transmission and distribution service areas as certain portions of the service territory continue to experience double digit customer growth. The Company is expanding in new areas that are expected to provide 8,000 potential new customers from capital invested between 1997 and 1999. The

Company partnered with local economic development agencies to attract controlled agriculture to the service territory. The first hydroponics facility was placed in eastern Arizona in mid 1998. The Company anticipates that additional hydroponics facilities will be placed in service during 1999.

In November 1998, Castle and Cooke Properties, Inc. (Castle) filed a complaint for recovery of response costs, contribution under CERCLA and under the Hawaii Environmental Response Law, statutory and equitable indemnity, damages and injunctive relief for trespass and nuisance, damages for negligence, and declaratory relief arising out of the alleged environmental contamination of real property located adjacent to the former gas plant site. Castle alleges that hazardous chemicals and certain petroleum products migrated from the BHP Iwilei Road property to the adjacent Castle property. Since BHP Hawaii has retained ownership of the Iwilei Road property and has indemnified the Company for environmental liabilities related to this property, it is expected that the outcome of the litigation will result in no judgment against the Company.

In 1995, the Hawaii Department of Health (HDOH) issued notices requesting information from current property owners and facility operators around Honolulu Harbor relating to the HDOH's intent to conduct a regional assessment of environmental conditions under authority of the Hawaii Environmental Response Law. Information relating to two sites within the assessment area was provided to HDOH by BHP Gas Company. On October 31, 1997, BHP Gas Company (Gasco, Inc.) was acquired by the Company, and is now operated as The Gas Company, a division of Citizens Utilities Company. The two sites in the assessment area are Gasco, Inc's former gas plant site at 616 Iwilei Road and the Company's leased facilities at Pier 38. Site specific cleanup was completed at Pier 38 and a "no further action" letter was obtained from the HDOH prior to the Company's acquisition of Gasco, Inc. The former gas plant site on Iwilei Road was purchased by BHP Hawaii from Gasco, Inc. prior to the Company's acquisition of Gasco, Inc. Furthermore, BHP Hawaii provided to the Company a complete indemnity from all environmental claims related to the Iwilei Road property. This indemnity is guaranteed by BHP Hawaii's parent, Broken Hill Proprietary, Ltd., an Australian company.

#### *Electric*

Operating divisions of the Company provide electric transmission and distribution services to the following approximate number of primarily residential customers in the following states:

<u>State</u>	<u>Customers</u>
Arizona	65,100
Hawaii	29,800
Vermont	20,500
Total	<u>115,400</u>

The provision of services and/or rates charged are subject to the jurisdiction of federal and state regulatory agencies. The Company purchases approximately 81% of needed electric energy, the supply of which is believed to be adequate to meet current demands and to provide for additional sales to new customers. The majority of the Company's generating facilities are on Kauai. The Company has smaller generating facilities in Arizona and Vermont which are used mainly for back-up power supply. Generally, the Company's electric sector does not experience material seasonal fluctuations.

The electric utility industry in the United States is undergoing fundamental changes. Electric utilities have for many years been vertically-integrated entities with the responsibility for the generation, transmission and distribution of electric power in a franchise territory. In return for monopoly status, electric utilities have been subject to comprehensive regulation at the state and federal level. The industry is now shifting toward electric customers being able to choose their energy provider much like telephone customers are able to choose their long distance provider. Generally, this involves splitting apart the generation and transmission of power from the remainder of the business, and having generators compete with one another in the sale of power directly to retail customers. The interconnected regional transmission grids will be operated independently, continuing as a federally regulated monopoly. Local transmission and distribution facilities would continue as state-regulated monopolies. The change in the industry is in various stages of development around the United States.

In December 1996, the Arizona Corporation Commission (ACC) issued Decision No. 59943 approving rules for a phased-in transition to a competitive retail electric power market beginning January 1, 1999. Under the plan, retail access will be phased in over four years with 20% of the load open to competition by 1999, 50% by 2001 and 100% by 2003. Stranded costs are expected to be recovered from ratepayers through a surcharge with both an energy and/or demand component. In January 1999, the ACC voted to temporarily stay the electric deregulation rules. The ACC delayed the move to a competitive electric market until issues such as pricing, market structure

and stranded costs can be resolved. The ACC plans to begin an intensive series of public hearings to fine tune the competition rules and expects to outline a process and timeframe for the transition to electric competition in Arizona.

In 1995, the Company's Arizona Electric Division was notified by the United States Environmental Protection Agency (USEPA) of it being a Potentially Responsible Party related to poly chlorinated biphenol shipments that the Company made to PCB Inc., sites located in Kansas City, Kansas and Kansas City, Missouri in the mid 1980s. These sites have been designated by the USEPA as Superfund Sites and are in the process of being evaluated for remediation. The Company is one of over 1,500 parties that sent material to the sites and is considered a de minimus participant. The Company responded to a number of data requests from USEPA related to its shipments. There has not yet been a determination of the total cost of the remediation of the sites and of particular parties, including the Company's share of the cost. The Company is currently engaged in settlement discussions among the parties. The Company has reached a de minimis settlement for one of the two pending claims, and it expects that settlement of the other will be finalized in the near future.

The Company's Kauai, Hawaii operation is a participant in a collaborative proceeding with approximately 15 other parties initiated by the Hawaii Public Utilities Commission (HPUC) on Electric Utility Competition and Investigation of the Electric Utility Infrastructure in the State of Hawaii. The parties filed executive summaries and final statements of position with the HPUC on November 19, 1998. The HPUC is expected to deliberate on the findings and issue a final decision and order in 1999 or later.

The Vermont Public Service Board (the VPSB) has opened a docket (No. 5854) into competition, customer choice and restructuring of the Vermont electric industry. The purpose of the investigation is to develop an information base, principles and policy bases to support legislative proposals and rule making by the VPSB. During 1997 and 1998, the Senate passed a bill to allow customers to purchase power on the open market but it was defeated in the State House of Representatives.

The General Affairs Committee in the House has advised Vermont Governor Howard Dean that serious consideration be given to consolidation of the 22 utilities in the State. The panel specifically recommended that consideration begin with the amalgamation of the Company's Vermont operations with Green Mountain Power and Central Vermont Public Service Corporation. The Company has signed a confidentiality and cooperation agreement with Green Mountain Power and Central Vermont Public Service Corporation to permit an exchange of information to evaluate the possibility of consolidating the Vermont operations of the three utilities. In addition, consideration may be given to converting Vermont's investor owned utilities into a cooperative ownership structure. The Company will work with the VPSB and other parties to implement an appropriate plan, however, it is uncertain at this time whether the plan or its key elements including consolidation will ultimately be implemented.

The Vermont Joint Owners (VJO), a consortium of 14 Vermont utilities, including the Company, have entered into a purchase power agreement with Hydro-Quebec. The agreement contains "step-up" provisions that state that if any VJO member defaults on its obligation under the contract to purchase power from Hydro-Quebec the other VJO participants will assume responsibility for the defaulting party's share on a pro-rata basis. As of December 31, 1998, the Company's obligation under the agreement is approximately 10% of the total contract. The two largest participants in the VJO represent approximately 46% and 37% of the total contract, respectively. During 1998, these two major participants have each experienced regulatory disallowances that have resulted in credit rating downgrades and stock price declines. Both of these participants are in the process of appealing the regulatory disallowances; however, both companies have stated that an unfavorable ruling could jeopardize their ability to continue as going concerns. If either or both of these companies default on their obligations under the Hydro-Quebec agreement, the remaining members of the VJO, including the Company, may be required to pay for a substantially larger share of the VJO's total power purchase obligation for the remainder of the agreement. Such a result could have a materially adverse effect on the financial results of the Company's Vermont Electric Division and on the Company as a whole.

In January 1998, a power outage to approximately 5,000 customers in Vermont was caused by an ice storm. The costs related to power restoration was approximately \$3,000,000. The Company received insurance recovery for certain costs and has requested and received from the Vermont Public Service Board the ability to defer the remaining costs for potential recovery in future rate requests.

In November 1995, the Company's Vermont electric division was permitted an 8.5% rate increase. Subsequently, the VPSB called into question the level of rates awarded the Company in connection with its formal review of allegations made by the Department of Public Service (the DPS), the consumer advocate in Vermont and a former Citizens employee. The major issues in this proceeding involved classification of certain costs to property, plant

and equipment accounts and the Company's Demand Side Management program. In addition, the DPS believed that the Company should have sought and received regulatory approvals prior to construction of certain facilities in prior years. On June 16, 1997, the VPSB ordered the Company to reduce its rates for Vermont electric service by 14.65% retroactive to November 1, 1995 and to refund to customers, with interest, all amounts collected since that time in excess of the rates authorized by the VPSB. The Company estimates that the annual effect of the rate reduction ordered by the VPSB is approximately \$3.9 million. The Company made a \$6.6 million refund to its customers in 1997 by issuing a credit to the utility bills of each customer. In addition, the VPSB assessed statutory penalties totaling \$60,000 and placed the Company on regulatory probation for a period of at least five years. During this probationary period, the Company could lose its franchise to operate in Vermont if it violates the terms of probation prescribed by the VPSB. The VPSB prescribed final terms of probation in its final order issued September 15, 1998. In October 1998, the Company filed an appeal in the Vermont Supreme Court challenging certain of the penalties imposed by the VPSB.

*Water and Wastewater*

Through subsidiaries, the Company provides water distribution, wholesale water transmission, wastewater treatment, public works consulting and marketing and billing services to the following approximate number of primarily residential customers in the following states:

<u>State</u>	<u>Customers</u>
Arizona	115,000
Illinois	71,700
California	60,000
Pennsylvania	31,800
Ohio	14,900
Indiana	<u>1,300</u>
Total	<u>294,700</u>

The provision of services and/or rates charged are subject to the jurisdiction of federal and state regulatory agencies. A significant portion of the Company's water/wastewater treatment sector construction expenditures serving new customers are made under agreements with land developers who generally advance plant and/or funds for construction to the Company that are later refunded in part by the Company as new customers and revenues are added in the respective land developments.

In addition to increasing customers through agreements with land developers, the Company seeks to acquire water and/or wastewater operations from municipalities and private companies. Privatization opportunities are increasing as the water and wastewater industries in the United States continue to face significant changes due to increasing demands for advanced technical expertise and capital to meet the requirements of more stringent environmental regulations. Opportunities for public-private partnerships are demonstrated by the following factors: Water and wastewater industries continue to face significant challenges as environmental regulations rise and federal funding opportunities decline; there is a growing need for enhancement of existing infrastructure and construction of new facilities for water and wastewater systems; and there is an increased demand for government to restructure and decrease internal spending. The Company's geographic and service diversity and decades of experience in the water and wastewater industry provide a strong platform to successfully meet these needs and respond to the increasing trend for privatization. The Company plans to initially focus its privatization efforts in existing and surrounding service areas.

In October 1998, the Company agreed to acquire all of the stock of the Sorenson Utility Company (Sorenson) for approximately \$800,000. Sorenson provides wastewater collection and treatment for approximately 450 customers around Bullhead City, Arizona, which is adjacent to the Company's Mohave Water Division operations.

Pursuant to agreements with the Del Webb Corporation signed in September of 1997, the Company began providing construction water services to the master planned community of Anthem in September of 1998. Anthem is an approximately 5,700 acre master planned community located about 20 miles north of downtown Phoenix, Arizona. As currently planned, the project will consist of a mix of residential and commercial units which total approximately 14,500 equivalent residential units (ERUs). Development commenced in mid 1998 and home sales are scheduled to begin in March of 1999 with the first closing planned for August of 1999. On June 19, 1998, the Company was granted Certificates of Convenience and Necessity by the Arizona Corporation Commission for the approximately 5,700 acres of the project. The certificates are conditioned upon receiving franchises or

consents from Maricopa County for approximately 4,800 acres and the City of Phoenix for approximately 900 acres before June 19, 1999. The Company expects to receive the required franchise or consents.

In the first half of 1998, the Company conducted an extensive public planning process in its Sun City, Sun City West and Youngtown service areas. A Central Arizona Project (CAP) Task Force consisting of numerous customer groups evaluated various options for using CAP water in the communities and selected a CAP water use plan. On October 1, 1998, the Company applied to the Arizona Corporation Commission (ACC) to approve the CAP water use plan adopted by the CAP Task Force and to authorize a fee for recovery of deferred and ongoing costs related to its CAP subcontracts for the Sun City, Sun City West and Youngtown service areas. If approved by the ACC, all deferred costs would be recovered over a 42-month period and all ongoing costs related to the CAP subcontracts would be recovered as incurred. The Company would be required to fund approximately \$15 million in capital improvements needed to implement the water use plan over the next four years.

In November 1998, the Company received a complaint filed with the Illinois Commerce Commission by residents in certain subdivisions in Orland Township, IL. The residents allege that the Company has overcharged them for wastewater collection and treatment services from September 1995 to present. The residents have asked the Commission to investigate and reduce the Company's wastewater rates for their subdivisions and to refund overpayments for the period September 1995 to the date of the decision. On March 3, 1999, a Commission Hearing Examiner limited the residents potential claims to periods after November 16, 1996. The Company disagrees with the residents' position and believes that it has implemented rates in accordance with Commission Orders. Commission hearings will be scheduled in 1999.

Citizens Lake Water Company was created to deliver Lake Michigan water to wholesale public water supply customers. The target public water supplies are located primarily in southwest Cook County and northeast Will County, Illinois. This southwest suburban area targeted by the pipeline is one of the major growth corridors in the Chicago area. The Company has secured a Certificate of Convenience and Necessity to provide lake water to a 30-square mile service territory in this high growth region. The Company, pursuant to contracts, will swap assets with the neighboring Village of Bolingbrook which will add 6,000 water customers to the Company and service territory land capable of supporting 8,000 new customers.

In October 1998, the Company received an Order from the California Public Utilities Commission (CPUC) approving an increase in revenue of \$934,000 over two years. The revenue increase affected the Company's California water operations in its Felton, Larkfield and Sacramento Districts. The Order will increase the Company's water rates in California between 5% and 14% in two steps and went into effect on October 22, 1998.

The Company has been named as one of many defendants in two class actions pending against a variety of industrial companies and water providers in the Sacramento, CA area. Both actions involve the Company's California water property and the Company's compliance with providing potable water in accordance with established drinking water standards. Both cases have been stayed by the court (plaintiffs have appealed) pending the outcome of an Order Instituting Investigation (OII) by the CPUC.

In January 1999, the Company received an order from the Public Utility Commission of Ohio approving an increase in annual revenues of \$975,000.

## **General**

The Company's operations are conducted primarily in small and medium size towns and communities. No material part of the Company's business is dependent upon a single customer or small group of customers for its revenues. As a result of its diversification, the Company is not dependent upon any single geographic area for its revenues. Due to this diversity, no single regulatory body regulates a service of the Company accounting for more than 19% of its revenues.

The Company is subject to regulation by the respective local, state and federal regulatory agencies. The Company is not subject to the Public Utility Holding Company Act. Order backlog is not a significant consideration in the Company's business and the Company has no contracts or subcontracts which may be subject to renegotiation of profits or termination at the election of the federal government. The Company holds franchises from local governmental bodies which vary in duration. The Company also holds Certificates of Convenience and Necessity granted by various state commissions which are generally of indefinite duration. The Company has no special working capital practices. The Company's research and development activities are not material. There are no patents, trademarks, licenses or concessions held by the Company that are material.

The Company had approximately 6,700 employees at December 31, 1998.

The Year 2000 (Y2K) issue results from computer programs using a two-digit format, as opposed to four, to indicate the year. Such computer systems may be unable to interpret dates beyond the year 1999, which could cause system failures or other computer errors. For a detailed discussion regarding the Company's Y2K effort, see Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operation."

**(d) Financial Information about Foreign and Domestic Operations and Export Sales**

In 1995, the Company made an investment in and entered into definitive agreements with Hungarian Telephone and Cable Corp. (HTCC), a Delaware corporation, which owns and operates local telephone concessions in Hungary. In 1995 and 1996, the Company amended certain of such agreements and entered in additional agreements with HTCC regarding financial support provided by the Company. Such financial support agreements have since expired. In 1997, the Company acquired additional HTCC shares in the open market. Pursuant to the agreement, as amended, and such open market purchases, the Company (i) owns approximately 17% of the HTCC shares presently outstanding, (ii) has rights to purchase HTCC shares that, if fully exercised, would result in the Company owning a majority of HTCC common stock on a fully diluted basis, (iii) provided requested management services to HTCC on a cost-plus basis, and (iv) has the right to and has designated two members of the HTCC Board of Directors. The Company's investment in HTCC is classified as an available for sale security and accounted for using the cost method of accounting.

During 1997, HTCC disputed certain provisions of the agreement and the associated management fee. As a result, in September 1998, the current management services agreement was terminated and a new seven-year consulting services agreement between the Company and HTCC was entered into with services to begin in 2004. In return, HTCC issued to the Company 100,000 shares of its common stock and an \$8,400,000 note maturing in 2004 in settlement of the dispute with the Company.

The investment in HTCC has declined in value during 1998 and in the fourth quarter of 1998 management determined that the decline was other than temporary. As a result, the Company recognized a loss of \$31,900,000 in the HTCC investment as a reduction of Other income (loss), net in the statements of income and comprehensive income. This loss did not impact the Company's operating cash flows (see Note 16).

**Item 2. Description of Property**

The Administrative Office of the Company is located at 3 High Ridge Park, Stamford, Connecticut, 06905 and is leased. The operations support office for the Company's Communications businesses is located at 3 North Park East, 8800 North Central Expressway, Dallas, Texas, 75231 and is leased. The operations support office for the Company's CLEC business is located at 4400 NE 77<sup>th</sup> Avenue, Vancouver, Washington, 98662 and is owned. The operations support office for the Company's Public Service businesses is located at 1233 Westbank Expressway, Harvey, Louisiana, 70058 and is owned. In addition, the Company purchased a 30 acre site in Plano, Texas where a new operations support office is being constructed for the Company's Communications businesses. The Company also purchased a 25,000 sq. ft. office facility in the City of Flagstaff, Arizona which will serve as an additional operations support office for the Public Services businesses. The Company owns property including: telecommunications outside plant, central office, microwave radio and fiber-optic facilities; gas production, transmission and distribution facilities; electric generation, transmission and distribution facilities; water production, treatment, storage, transmission and distribution facilities; and wastewater treatment, transmission, collection and discharge facilities; all of which are necessary to provide services at the locations listed below.

<u>State</u>	<u>Service(s) Provided</u>
1. Arizona	Electric, Gas, Telecommunications*, Water, Wastewater
2. California	Telecommunications, Water
3. Colorado	Gas
4. Florida	Telecommunications
5. Hawaii	Electric, Gas
6. Idaho	Telecommunications
7. Illinois	Telecommunications, Water, Wastewater
8. Indiana	Water
9. Louisiana	Gas
10. Montana	Telecommunications
11. Nevada	Telecommunications

	<u>State</u>	<u>Service(s) Provided</u>
12.	New Mexico	Telecommunications
13.	New York	Telecommunications *
14.	Ohio	Water, Wastewater
15.	Oregon	Telecommunications
16.	Pennsylvania	Water
17.	Tennessee	Telecommunications
18.	Utah	Telecommunications
19.	Vermont	Electric
20.	Washington	Telecommunications
21.	West Virginia	Telecommunications*
22.	Wisconsin	Telecommunications*

\* Certain properties are subject to mortgage deeds pursuant to Rural Utilities Service borrowings.

### **Item 3. Legal Proceedings**

In 1995, the Company's Arizona Electric Division was notified by the United States Environmental Protection Agency (USEPA) of it being a Potentially Responsible Party related to poly chlorinated biphenol shipments that the Company made to PCB Inc., sites located in Kansas City, Kansas and Kansas City, Missouri in the mid 1980s. These sites have been designated by the USEPA as Superfund Sites and are in the process of being evaluated for remediation. The Company is one of over 1,500 parties that sent material to the sites and is considered a de minimus participant. The Company responded to a number of data requests from the USEPA related to its shipments. There has not yet been a determination of the total cost of the remediation of the sites and of particular parties, including the Company's share of the cost. The Company is currently engaged in settlement discussions among the parties. The Company has reached a de minimis settlement of one of the two pending claims, and it expects that settlement of the other will be finalized in the near future.

In November 1995, the Company's Vermont electric division was permitted an 8.5% rate increase. Subsequently, the VPSB called into question the level of rates awarded the Company in connection with its formal review of allegations made by the Department of Public Service (the DPS), the consumer advocate in Vermont and a former Citizens employee. The major issues in this proceeding involved classification of certain costs to property, plant and equipment accounts and the Company's Demand Side Management program. In addition, the DPS believed that the Company should have sought and received regulatory approvals prior to construction of certain facilities in prior years. On June 16, 1997, the VPSB ordered the Company to reduce its rates for Vermont electric service by 14.65% retroactive to November 1, 1995 and to refund to customers, with interest, all amounts collected since that time in excess of the rates authorized by the VPSB. The Company estimates that the future annual effect of the rate reduction ordered by the VPSB is approximately \$3.9 million. The Company made a \$6.6 million refund to its customers in 1997 by issuing a credit to the utility bills of each customer. In addition, the VPSB assessed statutory penalties totaling \$60,000 and placed the Company on regulatory probation for a period of at least five years. During this probationary period, the Company could lose its franchise to operate in Vermont if it violates the terms of probation prescribed by the VPSB. The VPSB prescribed final terms of probation in its final order issued September 15, 1998. In October 1998, the Company filed an appeal in the Vermont Supreme Court challenging certain of the penalties imposed by the VPSB.

In January 1997, the Company's Illinois subsidiary was served with a complaint in an action commenced by the Illinois Attorney General (the State). The complaint alleges violations of National Pollution Discharge Elimination System permits issued to three wastewater treatment plants, acquired in mid-1994 through a merger with Metro Utility Company (Metro), as well as related allegations. The majority of the alleged violations predate the Company's acquisition of the plants, one of which has been taken out of service to foster regionalization. The Company filed its answer denying the allegations of the complaint and raised the affirmative defense of failure of the State to comply with certain provisions of the Illinois Environmental Protection Act. A settlement has been completed with the Illinois Environmental Protection Agency by payment to the State of \$65,000. No determination of violation was reached. The Company has contractual rights of indemnification from the former shareholders of Metro. The Company has been compensated for its costs of settlement through settlement of these contractual rights and other claims against the shareholders of Metro.

In August 1997, a lawsuit was filed in the United States District Court for the District of Connecticut (Leventhal vs. Tow, et al.) against the Company and five of its officers, one of whom is also a director, on behalf of all persons

who purchased or otherwise acquired Series A and Series B shares of Common Stock of the Company between September 5, 1996 and July 11, 1997, inclusive. On February 9, 1998, the plaintiffs filed an amended complaint. The complaint alleges that Citizens and the individual defendants, during such period, violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 based upon certain public statements made by the Company, which are alleged to be materially false or misleading, or are alleged to have failed to disclose information necessary to make the statements made not false or misleading. The plaintiffs seek to recover unspecified compensatory damages. The Company and the individual defendants believe the allegations are unfounded and filed a motion to dismiss on March 27, 1998. On April 28, 1998 the plaintiffs served a Memorandum of Law in Opposition to Defendants Motion to Dismiss. Subsequent to that date, the parties filed reply memoranda. The court has the motion under consideration but has not yet established a schedule of oral arguments.

In March 1998, a lawsuit was filed in the United States District Court for the District of Connecticut (Ganino vs. Citizens Utilities Company, et al.), against the Company and three of its officers, one of whom is also a director, on behalf of all purchasers of the Company's common stock between May 6, 1996 and August 7, 1997, inclusive. The complaint alleges that the Company and the individual defendants, during such period, violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 by making materially false and misleading public statements concerning the Company's relationship with a purported affiliate, Hungarian Telephone and Cable Corp. (HTCC), and by failing to disclose material information necessary to render prior statements not misleading. The plaintiff seeks to recover unspecified compensatory damages. The Company and the individual defendants believe that the allegations are unfounded and have filed a motion to dismiss. The plaintiff requested leave to file an amended complaint and an amended complaint was served on the Company on July 24, 1998. The Company's motion to dismiss the amended complaint was filed on October 13, 1998. The court canceled scheduled oral argument for January 25, 1999 and has not yet reset a date for oral argument on the motion.

In November 1998, a class action lawsuit was filed in state District Court for Jefferson Parish, Louisiana, against the Company and three of its subsidiaries: LGS Natural Gas Company, LGS Intrastate, Inc. and Louisiana General Service Company. The lawsuit alleges that the Company and the other named defendants passed through in rates charged to Louisiana customers certain costs that plaintiffs contend were unlawful. The lawsuit seeks compensatory damages in the amount of the alleged overcharges and punitive damages equal to three times the amount of any compensatory damages, as allowed under Louisiana law. In addition, the Louisiana Public Service Commission has indicated its intention to open an investigation into the allegations raised in the lawsuit. The Company and its subsidiaries believe that the allegations made in the lawsuit are unfounded and the Company will vigorously defend its interests in both the lawsuit and the related Commission investigation.

In addition, the Company is party to various other legal proceedings arising in the normal course of business. The outcome of individual matters is not predictable. However, management believes that the ultimate resolution of all such matters, including those discussed above, after considering insurance coverages, will not have a material adverse effect on the Company's financial position, results of operations, or its cash flows.

#### **Item 4. Submission of Matters to Vote of Security Holders**

None in fourth quarter 1998.

##### **Executive Officers**

Information as to Executive Officers of the Company as of March 1, 1999 follows:

<u>Name</u>	<u>Age</u>	<u>Current Position and Office</u>
Leonard Tow	70	Chairman of the Board and Chief Executive Officer
Daryl A. Ferguson	60	President and Chief Operating Officer
Robert J. DeSantis	43	Chief Financial Officer, Vice President and Treasurer
O. Lee Jobe	41	Vice President, Communications; President, Citizens Communications Sector
J. Michael Love	47	Vice President, Public Services; President, Citizens Public Services Sector
L. Russell Mitten	47	Vice President, General Counsel and Assistant Secretary
James D. Ranton	43	Vice President, Corporate Human Resources
Livingston E. Ross	50	Vice President and Controller
David B. Sharkey	49	President, Electric Lightwave, Inc.
Donald P. Weinstein	34	Vice President, Planning and Development

There is no family relationship between any of the officers of the Registrant. The term of office of each of the foregoing officers of the Registrant will continue until the next annual meeting of the Board of Directors and until a successor has been elected and qualified.

**Leonard Tow** has been associated with the Registrant since April 1989 as a Director. In June 1990, he was elected Chairman of the Board and Chief Executive Officer. He was also Chief Financial Officer from October 1991 through November 1997. He has also been a Director and Chief Executive Officer of Century Communications Corp. since its incorporation in 1973 and Chairman of its Board of Directors since October 1989. He is Director of Hungarian Telephone and Cable Corporation, Chairman of the Board of Electric Lightwave, Inc. and is a Director of the United States Telephone Association.

**Daryl A. Ferguson** has been associated with the Registrant since July 1989. He has been President and Chief Operating Officer since July 1990. He is currently a Director of Hungarian Telephone and Cable Corporation and Chief Executive Officer and Vice Chairman of the Board of Electric Lightwave, Inc.

**Robert J. DeSantis** has been associated with the Registrant since January 1986. He has been Vice President and Treasurer since October 1991 and also has been Chief Financial Officer since November 1997. He is currently Chief Financial Officer, Vice President and Treasurer of Electric Lightwave, Inc.

**O. Lee Jobe** has been associated with the Registrant since July 1997. He was Vice President, Network Operations from July 1997 through October 1997. He has been Operating Vice President, Communications since October 1997. In January 1999 he was also appointed President, Citizens Communications Sector. Prior to joining the Registrant, he was Vice President, Business Operations at Pacific Bell from June 1994 through June 1997 and Director, Business Operations at Sprint Corporation from February 1990 to June 1994.

**J. Michael Love** has been associated with the Registrant since May 1990 and from November 1984 through January 1988. He was Vice President, Corporate Planning from March 1991 through January 1997. He was appointed Vice President, Public Services in January 1997. In January 1999, he was also appointed President, Citizens Public Services Sector.

**L. Russell Mitten** has been associated with the Registrant since June 1990. He was General Counsel until June 1991. He has been Vice President, General Counsel and Assistant Secretary since June 1991.

**James D. Ranton** has been associated with the Registrant since August 1996. Prior to joining the Registrant, he was Director of Compensation and Benefits at Carrier Corporation, a manufacturing company, from April 1993 to August 1996.

**Livingston E. Ross** has been associated with the Registrant since August 1977. He has been Vice President and Controller since December 1991.

**David B. Sharkey** has been associated with the Registrant since August 1994 and has been President of Electric Lightwave, Inc. since that date. He has been Chief Operating Officer of Electric Lightwave, Inc. since October 1997 and is Director of Electric Lightwave, Inc. Prior to joining the Registrant, he was Vice President and General Manager of Metromedia Paging, a wireless company headquartered in New Jersey, from August 1989 through July 1994.

**Donald P. Weinstein** has been associated with the Registrant since August 1989. He was Manager, Financial Planning from October 1992 through September 1996; and Director, Financial Planning from September 1996 through October 1997. He has been Vice President, Planning and Development since October 1997.

## **Part II**

### **Item 5. Market for the Registrant's Common Equity and Related Stockholder Matters**

#### **Price Range of Common Stock**

The Company's Common Stock is traded on the New York Stock Exchange under the symbol CZN. Prior to the conversion of the Company's Common Stock Series A into Common Stock Series B (now Common Stock) on August 25, 1997, the two series traded separately on the New York Stock Exchange under the symbols CZNA and CZN B, respectively. The following table indicates the high and low prices per share as taken from the daily quotations published in "The Wall Street Journal" during the periods indicated. Prices have been adjusted retroactively for subsequent stock dividends, rounded to the nearest 1/16th. (See Note 8 of Notes to Consolidated Financial Statements.)

	1st Quarter		2nd Quarter		3rd Quarter		4th Quarter	
	High	Low	High	Low	High	Low	High	Low
1998:								
CZN	\$10 <sup>7</sup> / <sub>8</sub>	\$8 <sup>7</sup> / <sub>8</sub>	\$11 <sup>3</sup> / <sub>16</sub>	\$9 <sup>1</sup> / <sub>2</sub>	\$10	\$6 <sup>7</sup> / <sub>8</sub>	\$ 9 <sup>1</sup> / <sub>16</sub>	\$7 <sup>1</sup> / <sub>4</sub>
1997:								
CZNA	\$11 <sup>1</sup> / <sub>16</sub>	\$9 <sup>13</sup> / <sub>16</sub>	\$11 <sup>1</sup> / <sub>2</sub>	\$8 <sup>5</sup> / <sub>16</sub>	N/A	N/A	N/A	N/A
CZNB	\$11 <sup>1</sup> / <sub>16</sub>	\$9 <sup>15</sup> / <sub>16</sub>	\$11 <sup>1</sup> / <sub>2</sub>	\$7 <sup>5</sup> / <sub>8</sub>	\$ 9	\$7 <sup>9</sup> / <sub>16</sub>	\$10 <sup>1</sup> / <sub>16</sub>	\$8 <sup>13</sup> / <sub>16</sub>

As of February 26, 1999, the approximate number of record security holders of the Company's Common Stock was 46,592. This information was obtained from the Company's transfer agent.

### Dividends

The amount and timing of dividends payable on Common Stock are within the sole discretion of the Company's Board of Directors. The Board of Directors has undertaken an extensive review of the Company's dividend policy in conjunction with its separation plans, which are discussed in detail in Item 1(a) of this report. Resulting from this review, in November 1998, the Board concluded that after the payment of the December 1998 stock dividend, the Company should discontinue the payment of stock dividends at least through the separation. Post-separation dividend policies for both the new company and Citizens Utilities Company will continue to be evaluated and will be subject to approval by each company's board of directors. In 1998 and 1997, the Board of Directors reviewed alternative stock dividend cash equivalents and associated stock dividend rates each quarter in order to determine and declare a prudent stock dividend rate in light of the Company's actual and forecasted financial position and results of operations, as well as dividend yields of comparable communications and public services companies. Quarterly stock dividends declared and issued on Common Stock were .75% for each quarter of 1998, 1.6% for the first and second quarters of 1997 and 1.0% for the third and fourth quarters of 1997. The stock dividend cash equivalents considered to determine the stock dividend rates, adjusted for all stock dividends paid subsequent to all dividends declared through December 31, 1998, and rounded to the nearest <sup>1</sup>/<sub>16</sub>th, were as follows:

	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
1998	6 <sup>1</sup> / <sub>16</sub> ¢	7 <sup>9</sup> / <sub>16</sub> ¢	7 <sup>7</sup> / <sub>16</sub> ¢	6 <sup>3</sup> / <sub>16</sub> ¢
1997	17 <sup>7</sup> / <sub>16</sub> ¢	16 <sup>1</sup> / <sub>16</sub> ¢	8 <sup>1</sup> / <sub>16</sub> ¢	9 <sup>7</sup> / <sub>16</sub> ¢

### Recent Sales of Unregistered Securities, Use of Proceeds from Registered Securities

None

### Item 6. Selected Financial Data (\$ in thousands, except for per-share amounts)

	Year Ended December 31,				
	1998	1997	1996	1995	1994
Revenues .....	\$1,542,372	\$1,393,619	\$1,306,517	\$1,069,032	\$906,150
Net income (1).....	\$ 57,060	\$ 10,100	\$ 178,660	\$ 159,536	\$143,997
Basic net income per-share of Common Stock (1)(2) .....	\$ .22	\$ .04	\$ .68	\$ .64	\$ .61
Stock dividends declared on Common Stock (3) .....	3.03%	5.30%	6.56%	6.35%	5.04%
	As of December 31,				
	1998	1997	1996	1995	1994
Total assets .....	\$5,292,932	\$4,872,852	\$4,523,148	\$3,918,187	\$3,576,566
Long-term debt .....	\$1,900,246	\$1,706,532	\$1,509,697	\$1,187,000	\$ 994,189
Equity (4) .....	\$1,994,021	\$1,880,461	\$1,879,433	\$1,559,913	\$1,156,896

- (1) Reflects the impact of special items in 1998 and 1997 and CLEC losses (See Net Income and Net Income per Common Share section of the Results of Operations in Management's Discussion and Analysis of Financial Condition and Results of Operations).
- (2) Adjusted for subsequent stock dividends.
- (3) Compounded annual rate of quarterly stock dividends.
- (4) Includes Company obligated mandatorily redeemable convertible preferred securities.

## **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

This annual report on Form 10-K contains forward-looking statements that are subject to risks and uncertainties which could cause actual results to differ materially from those expressed or implied in the statements. All forward-looking statements (including oral representations) are only predictions or statements of current plans, which are constantly under review by the Company. All forward-looking statements may differ from actual future results due to, but not limited to, changes in the economy of the Company's markets, the nature and pace of technological changes, the number and effectiveness of competitors in the Company's markets, weather conditions, changes in legal and regulatory policy, success in overall strategy, the Company's ability to identify future markets and successfully expand existing ones, the mix of products and services offered in the Company's target markets, Y2K issues and the effects of the separation. Readers should consider these important factors in evaluating any statement in this Form 10-K or other wise made by the Company or on its behalf. The following information should be read in conjunction with the consolidated financial statements and related notes to the consolidated financial statements included in this report. The Company has no obligation to update or revise these forward-looking statements to reflect the occurrence of future events or circumstances.

On May 18, 1998, the Company announced its plans to separate its telecommunications businesses and public services businesses into two stand-alone publicly-traded companies. The Company intends to establish and transfer to a new company all of its telecommunications businesses, including its approximate 83% interest in Electric Lightwave, Inc. (ELI). This separation is subject to federal and state regulatory approvals and final Board approval, and is expected to be carried out through a distribution in the stock of the new company to the Company's shareholders. The public services businesses will continue to operate as Citizens Utilities Company and intend to provide gas transmission and distribution, electric transmission and distribution, water distribution and wastewater treatment services. This separation is being made in recognition of the different investment features, performance criteria, capital structures, dividend policies, customers' requirements and regulatory designs of each business, and would allow each business to pursue its own strategy and compete more effectively in its respective markets. The separation is expected to strengthen both businesses and enable them to take full advantage of opportunities to enhance value.

The Company received an order from the Federal Energy Regulatory Commission that granted an approval necessary to proceed with its separation plans. The Company filed a request with the Internal Revenue Service for a private letter ruling that the transaction is not subject to federal income tax. The Company has filed petitions with numerous state regulatory agencies for the approvals necessary to proceed with its separation plans and to date has received the necessary approval from four of these agencies. An application with the Federal Communications Commission (FCC) for the transfer of certain licenses and filings with the Securities and Exchange Commission will also be made during the separation process. The transaction is expected to be completed in the second half of 1999.

Although the Company continues to aggressively pursue its separation plans, changing market conditions and new business opportunities may require it to consider other methods to enhance shareholder value, including the sale or other disposition of certain properties and the acquisition of new properties.

### **(a) Liquidity and Capital Resources**

The Company considers its operating cash flows and its ability to raise debt and equity capital as the principal indicators of its liquidity. The Company has committed lines of credit with commercial banks under which it may borrow up to \$575,000,000. There were no amounts outstanding under these lines at December 31, 1998. ELI has committed lines of credit with commercial banks under which it may borrow up to \$400,000,000. The Company has guaranteed all of ELI's obligations under these lines of credit. As of December 31, 1998, \$284,000,000 was outstanding under ELI's lines of credit.

Net capital expenditures, by sector, have been and are budgeted as follows:

	Budget	Actual		
	1999	1998	1997	1996
		(\$ in thousands)		
Gas .....	\$ 42,600	\$ 45,800	\$ 47,900	\$ 27,700
Electric .....	21,700	18,900	23,600	24,600
Water and Wastewater .....	25,700	30,800	32,200	21,000
Public Services.....	\$ 90,000	\$ 95,500	\$103,700	\$ 73,300
Communications (1) .....	269,000	201,400	263,000	184,000
CLEC (2) .....	261,000	200,000	124,500	41,600
General .....	20,000	25,100	33,300	18,900
	<u>\$640,000</u>	<u>\$522,000</u>	<u>\$524,500</u>	<u>\$317,800</u>

(1) Includes approximately \$30,500,000 and \$7,700,000 in 1999 and 1998, respectively, for the construction of an operations support office.

(2) Includes \$45,000,000 of non-cash capital lease additions in 1999.

The Company anticipates that the funds necessary for its 1999 capital expenditures will be provided from operations; from requisitions of Industrial Development Revenue Bond construction fund trust accounts; from advances of Rural Utilities Service loan contracts; from commercial paper notes payable; from parties desiring utility service; from debt, equity and other financing at appropriate times; and from short-term borrowings under bank credit facilities.

In June 1998, the Company arranged for the issuance of \$20,000,000 of Industrial Development Revenue Bonds with an interest rate of 5.45% and a maturity date of June 1, 2033. The proceeds will be used to fund the construction of the Company's gas facilities located in Yavapai County, Arizona.

#### *Investments and Acquisitions*

In March 1999, Adelphia Communications Corporation (Adelphia) and Century Communications Corp. (Century) announced the signing of a definitive agreement for the merger of Century with Adelphia. The Company currently owns 1,807,095 shares of Century Class A Common Stock. Pursuant to the Merger Agreement, each Century Class A Common share will be exchanged for cash of \$9.16 and .6122 of a share of Adelphia Class A Common Stock (for a total market value of \$44.14 per Century Class A Common share based on Adelphia's March 4, 1999 closing price of \$57 $\frac{1}{8}$ ).

In January 1999, Centennial Cellular Corp. (Centennial), was acquired as a result of its merger with CCW Acquisition Corp., a company organized at the direction of Welsh, Carson, Anderson & Stowe. The Company was a holder of 1,982,294 shares of Centennial Class B Common Stock. In addition, as a holder of 102,187 shares of Mandatorily Redeemable Convertible Preferred Stock (Preferred Security) of Centennial, the Company was required to convert the Preferred Security into approximately 2,972,000 shares of Class B Common Stock. In exchange for all of its common stock interests, the Company received approximately \$223,100,000 in cash, of which approximately \$17,500,000 related to accrued dividends on the preferred stock. The Company recorded a pre-tax gain of approximately \$69,500,000 on this transaction in January 1999.

The investment in HTCC declined in value during 1998 and in the fourth quarter of 1998 management determined that the decline was other than temporary. As a result, the Company recognized a loss of \$31,900,000 in the HTCC investment as a reduction of Other income (loss), net in the statements of income and comprehensive income.

In November 1998, the Company acquired all the stock of Rhinelander Telecommunications, Inc. (RTI) for approximately \$84,000,000 in cash. RTI is a diversified telecommunications company engaged in providing local exchange, long distance, Internet access, wireless and cable television services to rural markets in Wisconsin.

In October 1998, the Company agreed to acquire all of the stock of the Sorenson Utility Company (Sorenson) for approximately \$800,000. Sorenson provides wastewater collection and treatment for approximately 450 customers around Bullhead City, Arizona, which is adjacent to the Company's Mohave Water Division operations.

In October 1998, the Company acquired St. Charles Natural Gas Company for \$5,000,000 in cash. St. Charles Natural Gas Company is a natural gas distribution company serving 5,000 customers in Louisiana and will become part of the Company's Louisiana Gas Services operations.

In January 1998, the Company purchased 1,330,000 shares of D&E Communications (D&E) for approximately \$27,000,000 in cash. As of December 31, 1998 the investment represented 17.9% of D&E's outstanding common stock. D&E is a full-service telecommunications company in Lancaster County, Pennsylvania that offers both local and long distance service, wireless service, Internet service, paging, voice, data and video communications equipment and computer networking services. D&E is classified as an available for sale security and accounted for using the cost method of accounting.

## **Regulatory Environment**

### *Communications*

With the passage of the Telecommunications Act of 1996 (the 1996 Act) (see Item 1(c) for a detailed discussion of the 1996 Act), the national public policy framework for telecommunications was changed. A central focus for this sweeping policy reform was to open local telecommunications markets to workable competition. Pursuant to the requirements of the 1996 Act, the FCC has been and will be conducting rule-making proceedings resulting in a number of new rules that could negatively impact the operations of the Company's Communications sector. However, ELI has substantially expanded the breadth of its product offering and its geographic reach as a result of the 1996 Act which increased customer demand for enhanced broadband data services and the development of competitive public data and voice networks.

### *Electric*

The electric industry is moving toward deregulation, where customers will be able to choose their energy provider. This process is in various stages of development in the different states where the Company provides this service. Deregulation could potentially result in stranded plant investments, stranded costs for supply contracts and stranded costs associated with programs which promote the most efficient use of electricity and reduce the environmental impact of generation facilities. The Company believes there are many uncertainties associated with a restructuring of the electric utility industry.

The Vermont Joint Owners (VJO), a consortium of 14 Vermont utilities, including the Company, have entered into a purchase power agreement with Hydro-Quebec. The agreement contains "step-up" provisions that state that if any VJO member defaults on its obligation under the contract to purchase power from Hydro-Quebec the other VJO participants will assume responsibility for the defaulting party's share on a pro-rata basis. As of December 31, 1998, the Company's obligation under the agreement is approximately 10% of the total contract. The two largest participants in the VJO represent approximately 46% and 37% of the total contract, respectively. During 1998, these two major participants have each experienced regulatory disallowances that have resulted in credit rating downgrades and stock price declines. Both of these participants are in the process of appealing the regulatory disallowances; however, both companies have stated that an unfavorable ruling could jeopardize their ability to continue as going concerns. If either or both of these companies default on their obligations under the Hydro-Quebec agreement, the remaining members of the VJO, including the Company, may be required to pay for a substantially larger share of the VJO's total power purchase obligation for the remainder of the agreement. Such a result could have a materially adverse effect on the financial results of the Company's Vermont Electric Division and on the Company as a whole.

### *Water and Wastewater*

Privatization opportunities are increasing as the water and wastewater industries in the United States continue to face significant changes due to increasing demands for advanced technical expertise and capital to meet the requirements of more stringent environmental regulations. Over the past few years, there have been several efforts to remove federal barriers to privatization. The Company's geographic and service diversity and decades of experience in the water and wastewater industry provide a strong platform to successfully meet these needs and respond to the increasing trend for privatization. The Company plans to initially focus its privatization efforts in existing and surrounding service areas.

*Rate Increases*

In January 1999, the Company was authorized increases in annual revenues from regulatory commissions in Ohio totaling approximately \$975,000. In October 1998, the Company was authorized increases in annual revenues from regulatory commissions in California totaling approximately \$934,000.

*Impact of Year 2000*

The Y2K issue results from computer programs using a two-digit format, as opposed to four, to indicate the year. Such computer systems may be unable to interpret dates beyond the year 1999, which could cause system failures or other computer errors. In late 1997, the Company developed a four-phase program to address the Y2K issue. The four-phase program was designed to protect the safety and continuity of the Company's service delivery and support capabilities, computer systems and other critical functions. The Company's Y2K program seeks to address problems that could arise: (1) in Information Technology (IT) areas including information systems and technologies; (2) in non-IT areas such as telecommunications networks and switches, utility control and monitoring systems, premises, facilities and general business equipment; and (3) due to suppliers of products and services not being Y2K compliant. Phase I is inventory and identification of those systems with which the Company has exposure to Y2K issues. Phase II is the assessment and development of action plans. Phase III is the implementation of the Y2K remediation plans. Phase IV, which in some instances will run concurrent with Phase III, is the testing and validation of each remedial action to ensure compliance. This phase includes, in some cases, testing in an environment identical to, but separate from, the production environment. Each of the Company's sectors has a program office that manages the progress of the Y2K efforts. The Company has determined priorities for taking corrective actions on mission critical systems or products so as to ensure continued delivery of core business activities.

The Company is and will continue to use both internal and external resources to reprogram, replace and test software and address remediation of IT and non-IT operational assets for Y2K compliance. The Company has contracted with consulting firms to provide direction, support, methodologies, reporting standards and templates.

The following table includes information, by Phase, related to the Y2K program for both the Company's sectors:

	Estimated Completion Dates for Mission Critical Systems and Products	% Completed	Expenditures		
			Actual to Dec. 31, 1998	Estimated for 1999	Estimated to Dec. 31, 1999
<b>Telecommunications and Corporate</b>					
IT .....			\$5,969,000	\$17,192,000	\$23,161,000
Inventory	Completed	100%			
Assessment	3/31/99	96%			
Remediation	6/30/99	50%			
Testing	6/30/99	8%			
Non-IT .....			142,000	2,284,000	2,426,000
Inventory	Completed	100%			
Assessment	3/31/99	90%			
Remediation	6/30/99	59%			
Testing	6/30/99	8%			
<b>Public Services</b>					
IT .....			1,207,000	1,339,000	2,546,000
Inventory	Completed	100%			
Assessment	Completed	100%			
Remediation	3/31/99	95%			
Testing	5/31/99	45%			
Non-IT .....			1,256,000	6,839,000	8,095,000
Inventory	Completed	100%			
Assessment	Completed	100%			
Remediation	3/31/99	73%			
Testing	6/30/99	43%			
Total .....			<u>\$8,574,000</u>	<u>\$27,654,000</u>	<u>\$36,228,000</u>

The Company is required to expense costs related to Y2K remediation. The timing of expenses may vary and is not necessarily indicative of readiness efforts or progress to date. Funding of the Y2K costs is expected to occur from operating cash flows, cash and investments and proceeds from the issuance of securities and/or other borrowings.

The systems of vendors and suppliers play a major role in the conduct of the business of the Company. As a result, in accordance with its Y2K program, the Company has been contacting software suppliers to determine major areas of exposure to Y2K issues. The Company has also been contacting its major suppliers and service providers to ascertain their ability to comply. In addition, the Company contracted with a consulting firm to review the Y2K programs of selected third party vendors. Thus far, most of these parties have stated that they intend to be Y2K compliant by the year 2000. However, there can be no guarantee that the systems of suppliers or service providers on which the Company's systems rely will be compliant, or that failure to be compliant by another company, or a conversion that is incompatible with the Company's systems, would not have a material adverse effect on the Company. The Company's Telecommunications businesses rely, directly and/or indirectly, on a large number of traffic carriers to carry telecommunications traffic through a series of interconnected chains of communications. Therefore, despite its efforts, the Company cannot ensure that each entity involved in the delivery of telecommunications services will be Y2K compliant. Furthermore, the electric power-supply systems of North America are connected into four major interconnections called grids. Operational component failures of any entity connected to any of the grids could cause failures in that grid. The Company will need to continue to assess these risks as the millennium approaches to evaluate the likelihood of failures and develop approaches for mitigating the risk of failures. In an effort to address third party compliance issues, the Company's Communications sector has initiated testing activities with one of its major suppliers.

In the event of non-remediation of the Y2K issues by the Company or certain of its vendors, the worst case scenario would be disruption of the Company's operations, possibly impacting the provision of services to customers and

the Company's ability to bill or collect revenues. However, management believes that the Company's efforts to mitigate its Y2K issues will avoid significant business interruptions. Contingency planning is an ongoing process. While the Company's overall Y2K contingency plan is now being devised, existing disaster recovery documentation and procedures remain the first line of defense. Some Y2K specific plans have been developed and are being reviewed and tested. All Y2K operational contingency plans are expected to be completed and tested by June 1999.

In addition, the Company participates in trade associations such as the Electric Power Research Institute (EPRI) and the American Gas Association (AGA), which furthers the industry's efforts toward Y2K readiness. The Company uses these organizations' Y2K programs' vast resources to accelerate its Y2K program for embedded systems. They also provide a forum for working within the industry peer group whereby joint conclusions may be reached on other key aspects of Y2K readiness. EPRI's Y2K program participants represent more than 70% of the electric power generation capacity in the U.S. AGA represents 181 natural gas utilities that deliver gas to homes and businesses in all fifty states.

The Company intends to complete its Y2K remediation efforts on mission critical systems and products so as to ensure continued delivery of core business activities by June 1999. Testing, remediation and monitoring will continue through the remainder of 1999 to verify that there are no outstanding problems that either were not captured during the initial Y2K efforts or arose after June 30, 1999. Also, review, modifications and testing of the contingency plans may and will occur throughout the remainder of 1999 and into the year 2000.

The extent and magnitude of the Y2K problem is difficult to predict or quantify. The above information is based on the Company's best estimates which were made using numerous assumptions, including the availability and future costs of certain technological and other resources, third party modification actions and other factors. Given the complexity of the issue and the possibility of unidentified risks, actual results may vary materially from those discussed above. Specific factors that might cause such differences include, among others, the availability and cost of the personnel trained in this area, the ability to locate and correct all affected computer codes, the timing and success of remedial efforts of third party suppliers and similar uncertainties.

A number of financial and information system applications have been identified as being Y2K compliant due to their recent implementation. The Company's core financial systems are being replaced pursuant to the information systems initiative discussed below.

#### *Other Information Systems Initiatives*

The Company also has information systems initiatives in process which are not the result of the Y2K initiative. These include implementation of an enterprise-wide financial system and the development of technology to bring the Company into full compliance with the Telecommunications Act of 1996 Interconnection Order. For these two projects, the Company expects to incur at least \$19,000,000 in costs over the next twelve months. The Company will be required to expense a portion of the cost of these projects under generally accepted accounting principles. For the year ended December 31, 1998, the Company incurred approximately \$31,000,000 in total costs in connection with these projects, of which approximately \$8,000,000 has been expensed.

#### *New Accounting Pronouncements*

In June 1998, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities" (SFAS 133). SFAS 133 requires companies to record derivatives on the balance sheet as assets or liabilities measured at fair value. Gains or losses resulting from changes in the values of those derivatives would be accounted for depending on the use of the derivative and whether it qualifies for hedge accounting. The key criterion for hedge accounting is that the hedging relationship must be highly effective in achieving offsetting changes in fair value or cash flows. This statement is effective for all fiscal quarters of all fiscal years beginning after June 15, 1999. The Company does not expect the adoption of SFAS 133 to have a material effect on the Company's financial position, operations or cash flows.

### **(b) Results of Operations**

#### **Revenues**

Total revenues increased \$148.8 million, or 11%, in 1998 and \$87.1 million, or 7%, in 1997. The increase in 1998 was primarily due to increases in communications, CLEC and gas revenues. The increase in revenues in 1997 was primarily due to increases in communications and CLEC revenues.

**Telecommunications revenues**

Telecommunications (communications and CLEC) revenues increased \$72.5 million, or 8%, in 1998 and \$74.0 million, or 9%, in 1997. The increase in 1998 was primarily due to increased network access services revenues in the communications sector and local telephone services revenues in the CLEC sector. The increase in 1997 was primarily due to increased local network and long distance services revenues in the communications sector and network and local telephone services revenues in the CLEC sector.

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
(\$ in thousands)					
<b>Communications revenues</b>					
Network access services .....	\$432,018	7%	\$403,990	3%	\$391,151
Local network services .....	262,239	5%	250,521	8%	232,904
Long distance services .....	96,584	6%	90,747	54%	59,072
Directory services .....	31,691	(1%)	31,982	6%	30,248
Other .....	44,914	(8%)	48,922	(2%)	50,084
Eliminations .....	(32,407)	37%	(23,573)	110%	(11,250)
Total .....	<u>\$835,039</u>	4%	<u>\$802,589</u>	7%	<u>\$752,209</u>

Network access services revenues increased \$28.0 million, or 7%, in 1998 primarily due to increases in special access revenues resulting from the introduction of the DS3 product, increased circuit demand due to Internet growth and increased minutes of use, partially offset by an FCC mandated interstate switched access rate reduction which became effective July 1, 1997. The network access services revenues increase in 1997 was primarily due to increased access minutes of use, partially offset by an FCC mandated interstate switched access rate reduction which became effective July 1, 1997.

Local network services revenues increased \$11.7 million, or 5%, in 1998 primarily due to business and residential access line growth and an increase in custom calling features and private line sales. The local network services revenues increase in 1997 was primarily due to communications acquisitions as well as internal access line growth.

Long distance services revenues increased \$5.8 million, or 6%, in 1998 primarily due to a 1997 charge of approximately \$14.2 million to revenues related to the curtailment of long distance service operations in adjacent markets. Absent the 1997 charge, long distance services revenues decreased 8% primarily due to the elimination of long distance product offerings to out-of-territory customers, partially offset by an increase in network usage for in-territory customers. The long distance services revenues increase in 1997 was primarily due to growth in customers and increased minutes of use, partially offset by the 1997 charge.

The directory services revenues increase in 1997 was primarily due to communications properties acquisitions and increased volume.

Other revenues decreased \$4.0 million, or 8%, in 1998 primarily due to the phasing out of certain surcharges resulting from rate case decisions in California and New York. The other revenues decrease in 1997 was primarily due to decreased billing and collection revenues.

Eliminations represent network access revenues received by the Company's local exchange operations from its long distance and competitive local exchange operations.

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
(\$ in thousands)					
<b>CLEC revenues</b>					
Network services .....	\$36,589	9%	\$33,522	68%	\$19,947
Local telephone services .....	38,169	261%	10,565	317%	2,533
Long distance services .....	12,309	51%	8,140	13%	7,232
Data services .....	13,813	56%	8,857	55%	5,705
Eliminations .....	<u>(3,061)</u>	(8%)	<u>(3,341)</u>	153%	<u>(1,319)</u>
Total .....	<u>\$97,819</u>	69%	<u>\$57,743</u>	69%	<u>\$34,098</u>

Network services revenues increased \$3.1 million, or 9%, in 1998 primarily due to increased revenues in new and existing markets. Existing market increases resulted from additional circuits sold. Increased revenues were partially offset by the expiration of a short-term contract with a significant customer. The network and strategic services revenues increase in 1997 was primarily due to sales of additional products to existing customers and an increase in route miles of 75% over 1996. Approximately \$6.8 million of the 1997 increase is associated with a short-term contract with a significant customer which expired in early 1998.

Local telephone services revenues increased \$27.6 million, or 261%, in 1998 primarily due to an increase in reciprocal compensation revenues, an increase in access line equivalents, and increased sales of the ISDN product. The Company's interconnection agreements expire in the second half of 1999. Management believes that these agreements will be replaced by agreements offering the Company some form of compensation regarding ISP traffic. There is no assurance, however, that the level of compensation will remain consistent with current levels, which could have a material adverse effect on the Company's revenue. The local telephone services revenues increase in 1997 was primarily due to local switch implementations for new and existing customers in the last half of 1996. The successful implementation of the ISDN PRI product generated approximately \$2.3 million of increased revenue in 1997.

Long distance services revenues increased \$4.2 million, or 51%, in 1998 primarily due to increases in prepaid services minutes processed resulting from new customers and increased revenues resulting from bundling of sales of long distance with other products. The increase in retail long distance revenues were offset by a decrease in wholesale long distance revenues primarily due to the loss of a large customer with credit problems. The long distance services revenues increase in 1997 was primarily due to increased prepaid debit card services introduced in late 1996 and growth associated with the local dial tone services market.

Data services revenues increased \$5.0 million, or 56%, in 1998 primarily due to an increase in sales of Internet, frame relay, and LAN/WAN services in new and existing markets, and new products such as ATM and Remote Net Connect. The data services revenues increase in 1997 was primarily due to a \$2.1 million increase in Internet access services revenues and \$1.6 million in frame relay revenue increases, partially offset by a decrease in other products. The Internet access service and frame relay revenue increases were primarily due to a 75% increase in Internet switches installed.

Eliminations reflect intercompany activity between the Company's CLEC and communications operations.

### Public services revenues

Public services revenues increased \$76.2 million, or 14%, in 1998 and \$13.1 million, or 3%, in 1997 primarily due to increased gas revenues.

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
(\$ in thousands)					
<b>Gas revenues</b>					
Residential .....	\$150,386	4%	\$145,016	8%	\$134,888
Commercial .....	109,259	71%	64,004	29%	49,633
Industrial .....	47,497	56%	30,366	(25%)	40,230
Municipal .....	<u>3,657</u>	12%	<u>3,251</u>	35%	<u>2,403</u>
Total distribution .....	310,799	28%	242,637	7%	227,154
Transportation .....	2,435	(7%)	2,622	(52%)	5,519
Other .....	<u>12,189</u>	78%	<u>6,839</u>	(2%)	<u>6,946</u>
Total .....	<u>\$325,423</u>	29%	<u>\$252,098</u>	5%	<u>\$239,619</u>

Gas revenues increased \$73.3 million, or 29%, in 1998 primarily due to the acquisition in October 1997 of Gasco, Inc., now known as The Gas Company (TGC), customer growth, increased residential and commercial consumption in Arizona, and increased industrial consumption in Louisiana, partially offset by a decrease in revenues resulting from warmer weather conditions and lower purchased gas costs passed on to customers in Louisiana. The gas revenues increase in 1997 was primarily due to higher gas prices, an increase in the number of customers, the acquisition of TGC and rate increases granted in Louisiana in May 1996 and Arizona in November 1996. This increase was partially offset by decreased industrial revenue as a result of a decrease in customers and lower consumption from high usage, low margin customers.

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
(\$ in thousands)					
<b>Electric revenues</b>					
Residential.....	\$ 80,887	1%	\$ 79,808	—	\$ 79,893
Commercial .....	57,617	3%	55,805	—	55,826
Industrial .....	39,393	(7%)	42,209	(4%)	44,165
Municipal .....	<u>8,265</u>	(3%)	<u>8,555</u>	5%	<u>8,175</u>
Total distribution .....	186,162	—	186,377	(1%)	188,059
Transmission.....	2,827	5%	2,694	15%	2,339
Other.....	<u>1,318</u>	(45%)	<u>2,399</u>	26%	<u>1,899</u>
Total .....	<u>\$190,307</u>	(1%)	<u>\$191,470</u>	—	<u>\$192,297</u>

Absent the 1997 charge to reflect a Vermont public utility commission order requiring refunds to customers of approximately \$6.6 million, electric revenues decreased \$7.8 million, or 4%, primarily due to lower fuel costs passed on to customers and a commission ordered rate reduction in Vermont. The electric revenues decrease in 1997 was primarily due to the 1997 charge which was partially offset by increased residential and commercial revenues generated from rate increases granted in Hawaii in August 1996 and Arizona in January 1997 and increased consumption.

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
(\$ in thousands)					
<b>Water and wastewater revenues</b>					
Residential distribution .....	\$76,167	8%	\$70,742	—	\$70,845
Commercial distribution .....	14,793	4%	14,212	3%	13,801
Industrial distribution .....	1,034	8%	961	14%	843
Other .....	1,790	(53%)	3,804	36%	2,805
Total .....	<u>\$93,784</u>	5%	<u>\$89,719</u>	2%	<u>\$88,294</u>

Water and wastewater revenues increased \$4.1 million, or 5%, in 1998 primarily due to increased consumption and customer growth in Arizona and Illinois and a rate increase in Pennsylvania. The water and wastewater revenues increase in 1997 was primarily due to an operating and maintenance service contract and a rate increase granted in Pennsylvania in June 1996.

#### Cost of Services

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
(\$ in thousands)					
Gas purchased .....	\$166,829	19%	\$139,900	9%	\$127,913
Network expenses .....	140,471	3%	136,971	77%	77,214
Electric energy and fuel oil purchased .....	87,930	(7%)	94,726	2%	93,191
Eliminations .....	<u>(35,468)</u>	32%	<u>(26,914)</u>	114%	<u>(12,569)</u>
Total .....	<u>\$359,762</u>	4%	<u>\$344,683</u>	21%	<u>\$285,749</u>

Gas purchased expense increased \$26.9 million, or 19%, in 1998 primarily due to the acquisition of TGC in October 1997 and an increase in customers in Arizona. The gas purchased expense increase in 1997 was primarily due to fluctuations in the price of gas, increased demand as a result of an increase in the number of customers and the acquisition of TGC in October 1997. Under tariff provisions, increases in the Company's costs of gas purchased are largely passed on to customers.

Network expenses increased \$3.5 million, or 3%, in 1998 primarily due to CLEC revenue growth, CLEC national data expansion efforts, and significant growth in CLEC long distance services. This increase was partially offset by an \$11.1 million 1997 charge related to lease terminations as a result of the curtailment of certain long distance service operations and lower negotiated rates in 1998. Absent the 1997 charge, network expenses increased 12% primarily due to CLEC revenue growth, CLEC national data expansion efforts, and significant growth in CLEC long distance services. The network expenses increase in 1997 was primarily due to an increase in long distance minutes sold requiring additional network access capacity and the 1997 charge.

Electric energy and fuel oil purchased decreased \$6.8 million, or 7%, in 1998 primarily due to lower supplier prices in Hawaii and Arizona. The electric energy and fuel oil purchased increase in 1997 was primarily due to higher supplier prices.

Eliminations represent network expenses incurred by the Company's long distance operation for services provided by its local exchange operations and intercompany activity between the Company's CLEC and communications operations.

## Depreciation Expense

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
	(\$ in thousands)				
Depreciation expense .....	\$257,844	9%	\$235,812	22%	\$193,733

Depreciation expense increased \$22.0 million, or 9%, in 1998 primarily due to the acquisition of TGC and increased property, plant and equipment. The depreciation expense increase in 1997 was primarily due to increased property, plant and equipment as a result of acquisitions and new construction.

## Other Operating Expenses

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
	(\$ in thousands)				
Operating and Maintenance expense .....	\$603,277	(7%)	\$650,363	60%	\$407,579
Taxes other than income .....	95,995	4%	92,026	14%	80,947
Sales and Marketing .....	<u>47,325</u>	(14%)	<u>54,893</u>	28%	<u>42,823</u>
Total .....	<u>\$746,597</u>	(6%)	<u>\$797,282</u>	50%	<u>\$531,349</u>

Operating and maintenance expense decreased \$47.1 million, or 7%, in 1998 primarily due to \$150.6 million of 1997 charges partially offset by the full year impact of the acquisition of TGC, increased CLEC operating costs and 1998 special items consisting of Y2K expense of \$8.6 million and separation costs of \$2.1 million. Absent the 1997 charges and 1998 special items, operating and maintenance expenses increased 19% primarily due to the full year impact of the acquisition of TGC and increased CLEC operating costs. The operating and maintenance expense increase in 1997 was primarily due to the acquisition of TGC, increased CLEC costs and the 1997 charges. The 1997 charges include approximately \$7 million related to the curtailment of certain long distance service operations, approximately \$34.7 million related to benefit plan curtailments and related regulatory assets, approximately \$67.4 million related to the write-off of communications information systems and software, approximately \$34.3 million related to regulatory commission orders in New York, Vermont and Arizona, approximately \$10.8 million related to accounting policy changes associated with ELI in preparation for its initial public offering and approximately \$2.7 million of other adjustments.

Taxes other than income increased \$4.0 million, or 4%, in 1998 primarily due to the acquisition of TGC and increased property taxes in Vermont. The taxes other than income increase in 1997 was primarily due to increased payroll, property and franchise taxes resulting from communications acquisitions, taxes associated with long distance operations and increased property taxes in Arizona, California, Louisiana and Pennsylvania.

Sales and marketing expenses decreased \$7.6 million, or 14%, in 1998 primarily due to an \$8.6 million 1997 charge related to the curtailment of certain long distance service operations. Absent the 1997 charge, sales and marketing expenses increased 2% primarily due to increases in personnel and related expenses to support expanded CLEC service offerings, partially offset by a reduced communications sales and marketing workforce. The sales and marketing expense increase in 1997 was primarily due to increased costs necessary to support an increased level of service offerings and the 1997 charge.

### Investment and Other Income

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
	(\$ in thousands)				
Non operating gain on sale of subsidiary stock .....	\$ —	N/A	\$ 78,734	N/A	\$ —
Investment income .....	32,505	(4%)	33,739	26%	26,834
Other income (loss), net .....	(24,526)	(704%)	4,062	(90%)	39,621
	<u>\$ 7,979</u>	(93%)	<u>\$116,535</u>	75%	<u>\$66,455</u>

The non operating gain on sale of subsidiary stock in 1997 of \$78.7 million represents the pre-tax gain on the ELI initial public offering of 8,000,000 shares of Class A Common Stock at a price of \$16 per share on November 24, 1997.

Investment income decreased \$1.2 million, or 4%, in 1998 primarily due to lower average investment balances. The investment income increase in 1997 was primarily due to higher investment balances and an increase in the Centennial dividend.

Other income (loss), net decreased \$28.6 million, or 704%, in 1998 primarily due to the recognition of a \$31.9 million loss resulting from the decline in value of the HTCC investment, partially offset by a 1997 charge of approximately \$4.5 million related to an Arizona Public Utility Commission order disallowing recovery of certain amounts of the equity component of the AFUDC. Absent the decline in value of HTCC and the 1997 charge, other income (loss), net decreased 14% primarily due to a decrease in the equity component of AFUDC. The other income (loss), net decrease in 1997 was primarily due to the 1997 charge, \$22 million earned from HTCC in 1996 for guarantees and financial support provided by the Company and 1996 gains totaling \$4.5 million on the sale of land in Illinois assets in Arizona.

### Minority Interest

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
	(\$ in thousands)				
Minority interest .....	\$14,032	2,076%	\$645	N/A	\$ —

Minority interest is a result of ELI's initial public offering in November 1997 and it represents 17.35%, as of December 31, 1998, of the minority's share of ELI's loss before income tax benefit and cumulative effect of a change in accounting principle.

### Interest Expense

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
	(\$ in thousands)				
Interest expense .....	\$112,239	3%	\$109,329	18%	\$92,695

Interest expense increased \$2.9 million, or 3%, in 1998 primarily due to increased long term debt outstanding partially offset by an increase in the debt component of AFUDC, a 1997 charge of approximately \$1.7 million related to an Arizona Public Utility Commission order disallowing recovery of certain amounts of the debt component of AFUDC. Absent the 1997 charge, interest expense increased 4% primarily due to increased long term debt outstanding, partially offset by an increase in the debt component of AFUDC. The interest expense increase in 1997 was primarily due to the issuance of debentures in June and December 1996 to fund acquisitions and capital expenditures and the 1997 charge.

## Income Taxes

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
	(\$ in thousands)				
Income taxes .....	\$22,337	203%	\$7,383	(91%)	\$84,937

Income taxes increased \$15.0 million, or 203%, in 1998 and decreased in 1997 primarily due to the \$62.1 million tax benefit associated with the 1997 charges to earnings. The effective annual tax rate is approximately 27% and 31% in 1998 and 1997, respectively.

## Net Income and Net Income Per Common Share

	1998		1997		1996
	Amount	Change from Prior year	Amount	Change from Prior year	Amount
	(\$ in thousands)				
Net Income .....	\$57,060	465%	\$10,100	(94%)	\$178,660
Net Income Per Share .....	\$ .22	450%	\$ .04	(94%)	\$ .68

1998 net income and net income per share were impacted by the following after tax items: Net losses from the Company's CLEC subsidiary of \$34.7 million, or 14¢ per share, the non-cash write down of the Company's investment in HTCC of \$19.7 million, or 7¢ per share, the cumulative effect of a change in accounting principle at the CLEC sector of \$2.3 million, or 1¢ per share, Y2K costs and separation costs of \$6.6 million, or 3¢ per share. Absent the impact of losses from the Company's CLEC subsidiary and the 1998 special items, net income would have been \$120.4 million, or 47¢ per share.

1997 net income and net income per share were impacted by the following after tax items: Net losses from the Company's CLEC subsidiary of \$23.8 million, or 9¢ per share, 1997 charges to earnings (see below) of \$135.2 million, or 52¢ per share, and a gain of \$51.2 million, or 20¢ per share, on the sale of stock by a subsidiary. Absent the impact of losses from the Company's CLEC subsidiary and the 1997 special items, net income would have been \$117.9 million, or 45¢ per share.

### 1997 Charges to Earnings

In 1996 and early 1997, the Company had been pursuing an aggressive growth strategy to take advantage of opportunities in the emerging communications marketplace. This strategy included the initiation and expansion of long distance services which, in combination with other enhanced service offerings, would enable the Company to offer an integrated package of products and services.

Late in 1996, the Company began the transition of its long distance network, primarily to fixed cost leases, in order to achieve the lowest cost of providing long distance service. In addition, the Company initiated a brand recognition program to support the sales and marketing initiatives designed to increase the Company's market share. The increase in revenues resulting from this growth strategy, though significant, did not offset the resulting increase in incremental expenses from the branding, sales, and marketing initiatives. As a result, the Company's long distance service operations generated unexpected losses during the first half of 1997 which had an adverse impact on the Company's earnings and cash flow. During the second quarter 1997, management re-evaluated this growth strategy in light of this continuing impact on earnings and cash flow.

In connection with the re-evaluation of the Company's communications growth strategy, as well as a review of its employee benefit plans to determine if such plans were competitive with those provided in the industry, several public utility commission orders requiring the Company to record charges to earnings, and other charges to earnings related to certain accounting policy changes at ELI in anticipation of its initial public offering, the Company recorded approximately \$197,300,000 of charges to earnings in 1997 as follows:

	1997
	(In thousands)
Curtailement of certain long distance service operations .....	\$ 34,600
Benefit plan curtailments and related regulatory assets .....	34,700
Telecommunications information systems and software .....	67,400
Regulatory commission orders .....	47,200
Other .....	13,400
Total .....	<u>\$197,300</u>

**Item 7A. Quantitative and Qualitative Disclosures about Market Risk**

The Company is exposed to the impact of interest rate and market risks. In the normal course of business, the Company employs established policies, procedures and internal processes to manage its exposure to interest rate and market risks. The Company's objective in managing its interest rate risk is to limit the impact of interest rate changes on earnings and cash flows and to lower its overall borrowing costs. To achieve these objectives, the Company refinances debt when advantageous and maintains fixed rate debt on a majority of its borrowings. The Company maintains a portfolio of investments consisting of both equity and bond financial instruments. The Company's equity portfolio primarily includes long-term investments in telecommunications companies. The Company's conservative bond portfolio consists of fixed income, state and municipal securities. The Company does not hold or issue derivative or other financial instruments for trading purposes. The Company purchases monthly gas futures contracts to manage well-defined commodity price fluctuations, caused by weather and other unpredictable factors, associated with the Company's commitments to deliver natural gas to certain industrial customers at fixed prices. This derivative financial instrument activity is not material to the Company's consolidated financial position, results of operations or cash flows.

**Item 8. Financial Statements and Supplementary Data**

The following documents are filed as part of this Report:

1. Financial Statements, See Index on page F-1.
2. Supplementary Data, Quarterly Financial Data is included in the Financial Statements (see 1. above).

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None

**Part III**

The Company intends to file with the Commission a definitive proxy statement for the 1999 Annual Meeting of Stockholders pursuant to Regulation 14A not later than 120 days after December 31, 1998. The information called for by this Part III is incorporated by reference to that proxy statement.

**Part IV**

**Item 14. Exhibits, Financial Statement Schedules and Reports on Form 8-K**

(a) The exhibits listed below are filed as part of this Report:

<u>Exhibit No.</u>	<u>Description</u>
3.200.1	Restated Certificate of Incorporation of Citizens Utilities Company, with all amendments to June 6, 1996 and amendment dated May 21, 1998, (incorporated by reference to Exhibit 3.200.1 to the Registrant's Form S-3 filed June 27, 1996 and exhibit 3.200.1 to the Registrant's Quarterly Report on Form 10-Q for the six months ended June 30, 1998, respectively, File No. 001-11001).
3.200.2	By-laws of the Company, as amended to-date of Citizens Utilities Company, with all amendments to January 20, 1998, (incorporated by reference to Exhibit 3.200.2 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1997, File No. 001-11001).

<u>Exhibit No.</u>	<u>Description</u>
4.100.1	Indenture of Securities, dated as of August 15, 1991, to Chemical Bank, as Trustee, (incorporated by reference to Exhibit 4.100.1 to the Registrant's Quarterly Report on Form 10-Q for the nine months ended September 30, 1991, File No. 001-11001).
4.100.2	First Supplemental Indenture, dated August 15, 1991, (incorporated by reference to Exhibit 4.100.2 to the Registrant's Quarterly Report on Form 10-Q for the nine months ended September 30, 1991, File No. 001-11001).
4.100.3	Letter of Representations, dated August 20, 1991, from Citizens Utilities Company and Chemical Bank, as Trustee, to Depository Trust Company (DTC) for deposit of securities with DTC, (incorporated by reference to Exhibit 4.100.3 to the Registrant's Quarterly Report on Form 10-Q for the nine months ended September 30, 1991, File No. 001-11001).
4.100.4	Second Supplemental Indenture, dated January 15, 1992, to Chemical Bank, as Trustee, (incorporated by reference to Exhibit 4.100.4 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1991, File No. 001-11001).
4.100.5	Letter of Representations, dated January 29, 1992, from Citizens Utilities Company and Chemical Bank, as Trustee, to DTC, for deposit of securities with DTC, (incorporated by reference to Exhibit 4.100.5 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1991, File No. 001-11001).
4.100.6	Third Supplemental Indenture, dated April 15, 1994, to Chemical Bank, as Trustee, (incorporated by reference to Exhibit 4.100.6 to the Registrant's Form 8-K Current Report filed July 5, 1994, File No. 001-11001).
4.100.7	Fourth Supplemental Indenture, dated October 1, 1994, to Chemical Bank, as Trustee, (incorporated by reference to Exhibit 4.100.7 to Registrant's Form 8-K Current Report filed January 3, 1995, File No. 001-11001).
4.100.8	Fifth Supplemental Indenture, dated as of June 15, 1995, to Chemical Bank, as Trustee, (incorporated by reference to Exhibit 4.100.8 to Registrant's Form 8-K Current Report filed March 29, 1996, File No. 001-11001).
4.100.9	Sixth Supplemental Indenture, dated as of October 15, 1995, to Chemical Bank, as Trustee, (incorporated by reference to Exhibit 4.100.9 to Registrant's Form 8-K Current Report filed March 29, 1996, File No. 001-11001).
4.100.11	Seventh Supplemental Indenture, dated as of June 1, 1996, (incorporated by reference to Exhibit 4.100.11 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1996, File No. 001-11001).
4.100.12	Eighth Supplemental Indenture, dated as of December 1, 1996, (incorporated by reference to Exhibit 4.100.12 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1996, File No. 001-11001).
4.200.1	Indenture dated as of January 15, 1996, between Citizens Utilities Company and Chemical Bank, as indenture trustee (incorporated by reference to Exhibit 4.200.1 to the Registrant's Form 8-K Current Report filed May 28, 1996, File No. 001-11001).
4.200.2	First Supplemental Indenture dated as of January 15, 1996, between Citizens Utilities Company and Chemical Bank, as indenture trustee, (incorporated by reference to Exhibit 4.200.2 to the Registrant's Form 8-K Current Report filed May 28, 1996, File No. 001-11001).
4.200.3	5% Convertible Subordinated Debenture due 2036, (contained as Exhibit A to Exhibit 4.200.2), (incorporated by reference to Exhibit 4.200.2 to the Registrant's Form 8-K Current Report filed May 28, 1996, File No. 001-11001).
4.200.4	Amended and Restated Declaration of Trust dated as of January 15, 1996, of Citizens Utilities Trust, (incorporated by reference to Exhibit 4.200.4 to the Registrant's Form 8-K Current Report filed May 28, 1996, File No. 001-11001).
4.200.5	Convertible Preferred Security Certificate, (contained as Exhibit A-1 to Exhibit 4.200.4), (incorporated by reference to Exhibit 4.200.4 to the Registrant's Form 8-K Current Report filed May 28, 1996, File No. 001-11001).
4.200.6	Amended and Restated Limited Partnership Agreement dated as of January 15, 1996 of Citizens Utilities Capital L.P., (incorporated by reference to Exhibit 4.200.6 to the Registrant's Form 8-K Current Report filed May 28, 1996, File No. 001-11001).

<u>Exhibit No.</u>	<u>Description</u>
4.200.7	Partnership Preferred Security Certificate (contained as Annex A to Exhibit 4.200.6), (incorporated by reference to Exhibit 4.200.6 to the Registrant's Form 8-K Current Report filed May 28, 1996, File No. 001-11001).
4.200.8	Convertible Preferred Securities Guarantee Agreement dated as of January 15, 1996 between Citizens Utilities Company and Chemical Bank, as guarantee trustee, (incorporated by reference to Exhibit 4.200.8 to the Registrant's Form 8-K Current Report filed May 28, 1996, File No. 001-11001).
4.200.9	Partnership Preferred Securities Guarantee Agreement dated as of January 15, 1996 between Citizens Utilities Company and Chemical Bank, as guarantee trustee, (incorporated by reference to Exhibit 4.200.9 to the Registrant's Form 8-K Current Report filed May 28, 1996, File No. 001-11001).
4.200.10	Letter of Representations, dated January 18, 1996, from Citizens Utilities Company and Chemical Bank, as trustee, to DTC, for deposit of Convertible Preferred Securities with DTC, (incorporated by reference to Exhibit 4.200.10 to the Registrant's Form 8-K Current Report filed May 28, 1996, File No. 001-11001).
10.1	Incentive Deferred Compensation Plan, dated April 16, 1991, (incorporated by reference to Exhibit 10.1 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1991, File No. 001-11001).
10.6	Deferred Compensation Plans for Directors, dated November 26, 1984 and December 10, 1984, (incorporated by reference to Exhibit 10.6 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1984, File No. 001-11001).
10.6.1	Directors' Retirement Plan, effective January 1, 1989, (incorporated by reference to Exhibit 10.6.1 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1989, File No. 001-11001).
10.6.2	Non-Employee Directors' Deferred Fee Equity Plan dated as of June 28, 1994, with all amendments to May 5, 1997, (incorporated by reference to Exhibit A to the Registrant's Proxy Statement dated April 4, 1995 and Exhibit A to the Registrant's Proxy Statement dated March 28, 1997, respectively, File No. 001-11001).
10.16.1	Employment Agreement between Citizens Utilities Company and Leonard Tow, effective July 11, 1996, (incorporated by reference to Exhibit 10.16.1 to the Registrant's Quarterly Report on Form 10-Q for the nine months ended September 30, 1996, File No. 001-11001).
10.17	1992 Employee Stock Purchase Plan, with all amendments to May 5, 1997, (incorporated by reference to Exhibit 10.17 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1992, File No. 001-11001).
10.18	Amendments dated May 21, 1993 and May 5, 1997, to the 1992 Employee Stock Purchase Plan, (incorporated by reference to the Registrant's Proxy Statement dated March 31, 1993 and the Registrant's Proxy Statement dated March 28, 1997, respectively, File No. 001-11001).
10.20	Asset Purchase Agreements dated November 28, 1994, (incorporated by reference to Exhibit 10.20 to the Registrant's Annual Report on Form 10-K for the year ended December 31, 1994, File No. 001-11001).
10.21	1996 Equity Incentive Plan and amendment dated May 5, 1997 to 1996 Equity Incentive Plan, (incorporated by reference to Exhibit A to the Registrant's Proxy Statement dated March 29, 1996 and Exhibit B to Proxy Statement dated March 28, 1997, respectively, File No. 001-11001).
10.5	Participation Agreement between ELI, Shawmut Bank Connecticut, National Association, the Certificate Purchasers named therein, the Lenders named therein, BA Leasing & Capital Corporation and Citizens Utilities Company dated as of April 28, 1995, and the related operating documents (incorporated by reference to Exhibit 10.5 of ELI's Registration Statement on Form S-1 effective on November 21, 1997, File No. 333-35227).
12	Computation of ratio of earnings to fixed charges (this item is included herein for the sole purpose of incorporation by reference)
21	Subsidiaries of the Registrant
23	Auditors' Consent
24	Powers of Attorney
27	Financial Data Schedule

**Signatures**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

CITIZENS UTILITIES COMPANY  
(Registrant)

By: /s/ Leonard Tow

Leonard Tow  
Chairman of the Board; Chief Executive  
Officer; Member, Executive Committee  
and Director

March 11, 1999

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on the 11th day of March 1999.

<u>Signature</u>	<u>Title</u>
<u>/s/ Robert J. DeSantis</u> (Robert J. DeSantis)	Chief Financial Officer, Vice President and Treasurer
<u>/s/ Livingston E. Ross</u> (Livingston E. Ross)	Vice President and Controller
<u>Norman I. Botwinik*</u> (Norman I. Botwinik)	Director
<u>Aaron I. Fleischman*</u> (Aaron I. Fleischman)	Member, Executive Committee and Director
<u>James C. Goodale*</u> (James C. Goodale)	Director
<u>Stanley Harfenist*</u> (Stanley Harfenist)	Member, Executive Committee and Director
<u>Andrew N. Heine*</u> (Andrew N. Heine*)	Director
<u>John L. Schroeder*</u> (John L. Schroeder)	Member, Executive Committee and Director
<u>Robert D. Siff*</u> (Robert A. Siff)	Director
<u>Robert A. Stanger*</u> (Robert A. Stanger)	Director
<u>Edwin Tornberg*</u> (Edwin Tornberg)	Director
<u>Claire L. Tow*</u> (Claire L. Tow)	Director
<u>Charles H. Symington, Jr.*</u> (Charles H. Symington, Jr.)	Director

\*By: /s/ Robert J. DeSantis  
(Robert J. DeSantis)  
Attorney-in-Fact

Citizens Utilities Company and Subsidiaries

## Index to Consolidated Financial Statements

<u>Item</u>	<u>Page</u>
Independent Auditors' Report .....	F-2
Consolidated balance sheets as of December 31, 1998, 1997 and 1996 .....	F-3
Consolidated statements of income and comprehensive income for the years ended December 31, 1998, 1997 and 1996 .....	F-4
Consolidated statements of shareholders' equity for the years ended December 31, 1998, 1997 and 1996 .....	F-5
Consolidated statements of cash flows for the years ended December 31, 1998, 1997 and 1996 .....	F-6
Notes to consolidated financial statements .....	F-7

## **Independent Auditors' Report**

The Board of Directors and Shareholders  
Citizens Utilities Company:

We have audited the accompanying consolidated balance sheets of Citizens Utilities Company and subsidiaries as of December 31, 1998, 1997 and 1996, and the related consolidated statements of income and comprehensive income, shareholders' equity and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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 consolidated financial statements referred to above present fairly, in all material respects, the financial position of Citizens Utilities Company and subsidiaries as of December 31, 1998, 1997 and 1996, and the results of their operations and their cash flows for the years then ended in conformity with generally accepted accounting principles.

As discussed in Note 1(n) to the financial statements, the Company changed its method of accounting in 1998 to adopt the provisions of the American Institute of Certified Public Accountants Statement of Position (AICPA SOP) 98-1 "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use" and AICPA SOP 98-5 "Reporting on the Costs of Start-up Activities."

**KPMG LLP**

New York, New York  
March 5, 1999

Citizens Utilities Company and Subsidiaries

**Consolidated Balance Sheets**

December 31, 1998, 1997 and 1996

(\$ in thousands)	1998	1997	1996
<b>Assets</b>			
Current assets:			
Cash .....	\$ 31,922	\$ 35,163	\$ 24,230
Accounts receivable:			
Customers .....	251,374	239,226	198,138
Other .....	82,874	60,404	88,320
Less allowance for doubtful accounts .....	<u>15,870</u>	<u>22,225</u>	<u>4,808</u>
Net accounts receivable .....	318,378	277,405	281,650
Materials and supplies .....	29,249	19,885	27,159
Other current assets .....	<u>34,492</u>	<u>44,826</u>	<u>36,731</u>
Total current assets .....	<u>414,041</u>	<u>377,279</u>	<u>369,770</u>
Property, plant and equipment .....	5,947,353	5,297,737	4,582,869
Less accumulated depreciation .....	<u>1,898,730</u>	<u>1,629,944</u>	<u>1,444,817</u>
Net property, plant and equipment .....	<u>4,048,623</u>	<u>3,667,793</u>	<u>3,138,052</u>
Investments .....	414,761	398,499	539,152
Regulatory assets .....	204,703	209,921	193,779
Deferred debits and other assets .....	<u>210,804</u>	<u>219,360</u>	<u>282,395</u>
Total assets .....	<u>\$5,292,932</u>	<u>\$4,872,852</u>	<u>\$4,523,148</u>
<b>Liabilities and Shareholders' Equity</b>			
Current liabilities:			
Long-term debt due within one year .....	\$ 8,930	\$ 6,691	\$ 3,593
Short-term debt .....	110,000	—	—
Accounts payable .....	187,401	222,458	168,299
Income taxes accrued .....	53,599	45,064	90,317
Other taxes accrued .....	22,812	21,243	19,541
Interest accrued .....	27,645	25,413	24,522
Customers' deposits .....	33,668	22,095	21,400
Other current liabilities .....	<u>63,676</u>	<u>74,906</u>	<u>81,817</u>
Total current liabilities .....	507,731	417,870	409,489
Deferred income taxes .....	442,908	420,708	347,975
Customer advances for construction .....	211,941	174,858	154,324
Deferred credits .....	96,827	128,984	115,291
Contributions in aid of construction .....	90,353	85,932	84,129
Regulatory liabilities .....	19,120	20,881	22,810
Long-term debt .....	1,900,246	1,706,532	1,509,697
Minority interest in subsidiary .....	29,785	36,626	—
Company obligated mandatorily redeemable convertible preferred securities* .....	201,250	201,250	201,250
Shareholders' equity .....	<u>1,792,771</u>	<u>1,679,211</u>	<u>1,678,183</u>
Total liabilities and shareholders' equity .....	<u>\$5,292,932</u>	<u>\$4,872,852</u>	<u>\$4,523,148</u>

\* Represents securities of a subsidiary trust, the sole assets of which are securities of a subsidiary partnership, substantially all the assets of which are convertible debentures of the Company.

The accompanying Notes are an integral part of these Consolidated Financial Statements.

Citizens Utilities Company and Subsidiaries

**Consolidated Statements of Income and Comprehensive Income**

For the Years Ended December 31, 1998, 1997 and 1996

(\$ in thousands, except for per-share amounts)	1998	1997	1996
<b>Revenues</b>	\$1,542,372	\$1,393,619	\$1,306,517
<b>Operating expenses:</b>			
Cost of services .....	359,762	344,683	285,749
Operating and maintenance expenses .....	746,597	797,282	531,349
Depreciation .....	257,844	235,812	193,733
Total operating expenses .....	<u>1,364,203</u>	<u>1,377,777</u>	<u>1,010,831</u>
Income from operations .....	178,169	15,842	295,686
Non operating gain on sale of subsidiary stock .....	—	78,734	—
Investment income .....	32,505	33,739	26,834
Other income (loss), net .....	(24,526)	4,062	39,621
Minority interest .....	14,032	645	—
Interest expense .....	<u>112,239</u>	<u>109,329</u>	<u>92,695</u>
Income before income taxes, dividends on convertible preferred securities and cumulative effect of change in accounting principle .....	87,941	23,693	269,446
Income taxes .....	<u>22,337</u>	<u>7,383</u>	<u>84,937</u>
Income before dividends on convertible preferred securities and cumulative effect of change in accounting principle .....	65,604	16,310	184,509
Dividends on convertible preferred securities, net of income tax benefit .....	<u>6,210</u>	<u>6,210</u>	<u>5,849</u>
Income before cumulative effect of change in accounting principle .....	59,394	10,100	178,660
Cumulative effect of change in accounting principle, net of income tax benefit and related minority interest .....	<u>2,334</u>	<u>—</u>	<u>—</u>
Net income .....	57,060	10,100	178,660
Other comprehensive income, net of tax and reclassification adjustment .....	<u>52,872</u>	<u>10,832</u>	<u>(11,099)</u>
Total Comprehensive income .....	<u>\$ 109,932</u>	<u>\$ 20,932</u>	<u>\$ 167,561</u>
Net income per common share before cumulative effect of change in accounting principle:			
Basic .....	\$ .23	\$ .04	\$ .68
Diluted .....	\$ .23	\$ .04	\$ .68
Net income per common share:			
Basic .....	\$ .22	\$ .04	\$ .68
Diluted .....	\$ .22	\$ .04	\$ .68

The accompanying Notes are an integral part of these Consolidated Financial Statements.

Citizens Utilities Company and Subsidiaries

**Consolidated Statements of Shareholders' Equity**

For the Years Ended December 31, 1998, 1997 and 1996

(\$ in thousands, except for per-share amounts)	Common Stock (\$ .25)	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders' Equity
Balance January 1, 1996 .....	\$56,896	\$1,263,694	\$ 235,236	\$ 4,087	\$1,559,913
Acquisition .....	322	15,308			15,630
Common stock buybacks to fund stock dividends .....	(1,639)	(73,842)			(75,481)
Stock plans .....	330	6,959			7,289
Stock issuances to fund EPPICS dividends .....	178	7,621			7,799
EPPICS issuance cost .....		(4,528)			(4,528)
Net income .....			178,660		178,660
Other comprehensive income, net of tax and reclassification adjustment ...				(11,099)	(11,099)
Stock dividends in shares of Common Stock Series A and Series B .....	3,701	166,129	(169,830)		—
Balance December 31, 1996 .....	<u>\$59,788</u>	<u>\$1,381,341</u>	<u>\$ 244,066</u>	<u>\$ (7,012)</u>	<u>\$1,678,183</u>
Acquisitions .....	604	2,736	8,318		11,658
Common stock buybacks to fund stock dividends .....	(1,226)	(47,326)			(48,552)
Stock plans .....	188	6,380			6,568
Stock issuances to fund EPPICS dividends .....	247	10,175			10,422
Net income .....			10,100		10,100
Other comprehensive income, net of tax and reclassification adjustment ...				10,832	10,832
Stock dividends in shares of Common Stock .....	3,148	127,119	(130,267)		—
Balance December 31, 1997 .....	<u>\$62,749</u>	<u>\$1,480,425</u>	<u>\$ 132,217</u>	<u>\$ 3,820</u>	<u>\$1,679,211</u>
Acquisitions .....	133	2,150			2,283
Common stock buybacks to fund stock dividends .....	(453)	(14,370)			(14,823)
Stock plans .....	171	5,935			6,106
Stock issuances to fund EPPICS dividends .....	273	9,789			10,062
Net income .....			57,060		57,060
Other comprehensive income, net of tax and reclassification adjustment ...				52,872	52,872
Stock dividends in shares of Common Stock .....	1,914	70,259	(72,173)		—
Balance December 31, 1998 .....	<u>\$64,787</u>	<u>\$1,554,188</u>	<u>\$ 117,104</u>	<u>\$ 56,692</u>	<u>\$1,792,771</u>

The accompanying Notes are an integral part of these Consolidated Financial Statements.

Citizens Utilities Company and Subsidiaries

**Consolidated Statements of Cash Flows**

For the Years ended December 31, 1998, 1997 and 1996

(\$ in thousands)	1998	1997	1996
<b>Net cash provided by operating activities</b>	<u>\$ 262,368</u>	<u>\$ 230,432</u>	<u>\$ 375,181</u>
<b>Cash flows used for investing activities:</b>			
Securities matured .....	2,000	16,205	43,608
Securities sold .....	992,769	578,494	87,447
Securities purchased .....	(952,628)	(434,030)	(332,332)
Construction expenditures .....	(482,870)	(530,744)	(348,379)
Business acquisitions .....	(94,234)	(105,039)	(87,683)
Other .....	(1,028)	25,686	(47,802)
	<u>(535,991)</u>	<u>(449,428)</u>	<u>(685,141)</u>
<b>Cash flows from financing activities:</b>			
Long-term debt borrowings .....	243,404	159,769	351,053
Issuance of EPPICS .....	—	—	196,722
Issuance of common stock .....	7,101	4,825	6,049
Issuance of subsidiary stock .....	—	118,554	—
Short-term debt borrowings (repayments) .....	42,000	—	(140,650)
Common stock buybacks to fund stock dividends .....	(14,823)	(48,552)	(75,481)
Long-term debt principal payments .....	(7,300)	(3,287)	(20,243)
Other .....	—	(1,380)	(1,182)
	<u>270,382</u>	<u>229,929</u>	<u>316,268</u>
<b>Increase (decrease) in cash</b>	<u>(3,241)</u>	<u>10,933</u>	<u>6,308</u>
Cash at January 1, .....	<u>35,163</u>	<u>24,230</u>	<u>17,922</u>
Cash at December 31, .....	<u>\$ 31,922</u>	<u>\$ 35,163</u>	<u>\$ 24,230</u>

The accompanying Notes are an integral part of these Consolidated Financial Statements.

## Notes to Consolidated Financial Statements

### (1) Summary of Significant Accounting Policies:

#### (a) Description of Business:

The Company is a diversified communications and public services company which provides, either directly or through subsidiaries, telecommunications, gas transmission and distribution, electric transmission and distribution, water distribution and wastewater treatment services to customers in areas of 22 states. The Company is not dependent upon any single geographic area or single customer for its revenues. No single regulatory body regulated a service of the Company that accounted for more than 19% of its 1998 revenues.

On May 18, 1998, the Company announced its plans to separate its telecommunications businesses and public services businesses into two stand-alone publicly-traded companies. The Company intends to establish and transfer to a new company all of its telecommunications businesses, including its approximate 83% interest in Electric Lightwave, Inc. (ELI). This separation is subject to federal and state regulatory approvals and final Board approval, and is expected to be carried out through a distribution in the stock of the new company to the Company's shareholders. The public services businesses will continue to operate as Citizens Utilities Company and intend to provide gas transmission and distribution, electric transmission and distribution, water distribution and wastewater treatment services. This separation is being made in recognition of the different investment features, performance criteria, capital structures, dividend policies, customers' requirements and regulatory designs of each business, and would allow each business to pursue its own strategy and compete more effectively in its respective markets. The separation is expected to strengthen both businesses and enable each of them to take full advantage of opportunities to enhance value.

The Company received an order from the Federal Energy Regulatory Commission that granted an approval necessary to proceed with its separation plans. The Company filed a request with the Internal Revenue Service for a private letter ruling that the transaction is not subject to federal income tax. The Company has filed petitions with numerous state regulatory agencies for the approvals necessary to proceed with its separation plans and to date has received the necessary approval from four of these agencies. An application with the Federal Communications Commission (FCC) for the transfer of certain licenses and filings with the Securities and Exchange Commission will also be made during the separation process. The transaction is expected to be completed in the second half of 1999.

Although the Company continues to aggressively pursue its separation plans, changing market conditions and new business opportunities may require it to consider other methods to enhance shareholder value, including the sale or other disposition of certain properties and the acquisition of new properties.

#### (b) Principles of Consolidation and Use of Estimates:

The consolidated financial statements have been prepared in accordance with generally accepted accounting principles and include the accounts of Citizens Utilities Company and its subsidiaries. Certain reclassifications of balances previously reported have been made to conform to current presentation.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

#### (c) Revenues:

The Company records revenues from communications and public services customers when services are provided. Certain communications revenues are estimated under cost separation procedures that base revenues on current operating costs and investments in facilities to provide such services.

#### (d) Construction Costs and Maintenance Expense:

Property, plant and equipment are stated at original cost, including general overhead and an allowance for funds used during construction (AFUDC) for regulated businesses and capitalized interest for unregulated businesses. Maintenance and repairs are charged to operating expenses as incurred.

AFUDC represents the borrowing costs and a return on common equity of funds used to finance construction of regulated assets. AFUDC is capitalized as a component of additions to property, plant and equipment and is

**Notes to Consolidated Financial Statements—(Continued)**

credited to income. AFUDC does not represent current cash earnings; however, under established regulatory rate-making practices, after the related plant is placed in service, the Company is permitted to include in the rates charged for utility services a fair return on and depreciation of such AFUDC included in plant in service. The amount of AFUDC relating to equity is included in other income, net (\$5,311,000, \$6,881,000 and \$8,704,000 for 1998, 1997 and 1996, respectively) and the amount relating to borrowings is included as a reduction of interest expense (\$3,396,000, \$2,978,000 and \$3,385,000 for 1998, 1997 and 1996, respectively). The 1997 income statement also reflects a writeoff (\$4,486,000 relating to equity and \$1,744,000 relating to borrowings) pursuant to certain regulatory commission orders (see Note 10). The book value, net of salvage, of routine property, plant and equipment dispositions is charged against accumulated depreciation for regulated operations.

Capitalized interest for unregulated construction activities credited to interest expense related to ELI's capital expenditure program amounted to \$10,444,000, \$4,693,000 and \$3,109,000 for 1998, 1997 and 1996, respectively.

**(e) Depreciation Expense:**

Depreciation expense, calculated using the straight-line method, is based upon the estimated service lives of various classifications of property, plant and equipment and represents approximately 5%, 5% and 5% for 1998, 1997 and 1996, respectively, of the gross depreciable property, plant and equipment.

**(f) Regulatory Assets and Liabilities:**

The Company's regulated operations are subject to the provisions of Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation." SFAS 71 requires regulated entities to record regulatory assets and liabilities as a result of actions of regulators.

The Company continuously monitors the applicability of SFAS 71 to its regulated operations. SFAS 71 may, at some future date, be deemed inapplicable due to changes in the regulatory and competitive environments and/or a decision by the Company to accelerate deployment of new technology. If the Company were to discontinue the application of SFAS 71 to one or more of its regulated operations, the Company would be required to write off its regulatory assets and regulatory liabilities and would be required to adjust the carrying amount of any other assets, including property, plant and equipment, that would be deemed not recoverable related to those operations. In addition, there could be potential stranded costs associated with certain long term fixed price contracts which may not be recoverable. The Company believes its regulated operations continue to meet the criteria for SFAS 71 and that the carrying value of its regulated property, plant and equipment is recoverable in accordance with established rate-making practices.

**(g) Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of:**

The Company reviews long-lived assets and certain identifiable intangibles for impairment whenever events or changes in circumstances, including the actions of regulators, indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceed the fair value.

**(h) Accounting for Investments and Short-Term Debt:**

Investments include high credit quality, short- and intermediate-term fixed-income securities (primarily state and municipal debt obligations) and equity securities. The Company classifies its investments at purchase as available-for-sale or held-to-maturity in accordance with SFAS 115, "Accounting for Certain Investments in Debt and Equity Securities." The Company does not maintain a trading portfolio.

Securities classified as available-for-sale are carried at estimated fair market value. These securities are held for an indefinite period of time, but might be sold in the future as changes in market conditions or economic factors occur. Net aggregate unrealized gains and losses related to such securities, net of taxes, are included as a separate component of shareholders' equity. Securities classified as held-to-maturity are carried at amortized cost, adjusted for amortization of premiums/discounts and accretion over the period to maturity, and are those which the Company has the ability and intent to hold to maturity. Interest, dividends and gains and losses realized on sales of securities are reported in Investment income.

**Notes to Consolidated Financial Statements—(Continued)**

The Company evaluates its investments periodically to determine whether any decline in fair value, below the amortized cost basis, is other than temporary. If the Company determines that a decline in fair value is other than temporary, the cost basis of the individual investment is written down to fair value as a new cost basis and the amount of the write down is accounted for as a realized loss and included in earnings.

In 1998, short-term debt represents commercial paper notes payable. This short-term debt was repaid in January 1999 with the proceeds from the sale of the Company's investment in Centennial Cellular Corp. (Centennial) (see Note 1(i) below).

**(i) Investment in Centennial Cellular Corp.:**

In August 1991, the Company recorded its initial investment in 102,187 shares of Centennial Convertible Redeemable Preferred Stock (the Preferred Security) at \$49,842,000 and 1,367,099 shares of Centennial Class B Common Stock at \$19,826,000, which in the aggregate represented the historical cost of the Company's investment in its subsidiary, Citizens Cellular Company, prior to its merger with Centennial. During 1994, the Company purchased 615,195 additional shares of Centennial Class B Common Stock for \$8,613,000 pursuant to a Centennial rights offering.

The terms of the Preferred Security provided that the Preferred Security may be converted by the holder into Centennial common stock and that it accreted a liquidation value preference through August 31, 1996 at a fixed annual dividend rate of 7.5%, compounded quarterly, until the Preferred Security reached a liquidation value preference of \$186,287,000 on August 31, 1996.

The Company recognized the non-cash accretion on the Preferred Security as it was earned in each period through August 31, 1996 as investment income and increased the book value of its investment in Centennial by the same amount. The liquidation value preference earned on the Preferred Security for 1996 was \$9,043,000. From inception through August 31, 1996, \$57,837,000 of such accretion was accounted for in this manner. The Preferred Security was mandatorily redeemable on August 30, 2006.

Commencing September 1, 1996, Centennial had the option to either (a) declare and pay or accumulate an 8.5% annual dividend on the Preferred Security's \$186,287,000 liquidation value or (b) redeem the Preferred Security for \$186,287,000 in cash or in Centennial common stock. Commencing September 1, 1996, the Company recognized \$15,835,000, \$15,835,000 and \$5,278,000 as dividend income from Centennial related to 1998, 1997 and 1996, respectively.

In January 1999, Centennial was acquired as a result of its merger with CCW Acquisition Corp., a company organized at the direction of Welsh, Carson, Anderson & Stowe. The Company was a holder of 1,982,294 shares of Centennial Class B Common Stock. In addition, as a holder of 102,187 shares of Mandatorily Redeemable Convertible Preferred Stock of Centennial, the Company was required to convert the Preferred Security into approximately 2,972,000 shares of Class B Common Stock. In exchange for all of its common stock interests the Company received approximately \$223,100,000 in cash, of which approximately \$17,500,000 related to accrued dividends on the preferred stock. The Company recorded a pre-tax gain of approximately \$69,500,000 on this transaction in January 1999.

**(j) Income Taxes, Deferred Income Taxes and Investment Tax Credits:**

The Company and its subsidiaries are included in a consolidated federal income tax return. The Company utilizes the asset and liability method of accounting for income taxes. Under the asset and liability method, deferred income taxes are recorded for the tax effect of temporary differences between the financial statement and the tax bases of assets and liabilities using tax rates expected to be in effect when the temporary differences are expected to turn around. Regulatory assets and liabilities (see Note 1(f)) include income tax benefits previously flowed through to customers and from the allowance for funds used during construction, the effects of tax law changes and the tax benefit associated with unamortized deferred investment tax credits. These regulatory assets and liabilities represent the probable net increase in revenues that will be reflected through future ratemaking proceedings. The investment tax credits relating to utility properties, as defined by applicable regulatory authorities, have been deferred and are being amortized to income over the lives of the related properties.

**Notes to Consolidated Financial Statements—(Continued)**

**(k) Employee Stock Plans:**

The Company has various employee stock based compensation plans. Awards under these plans are granted to eligible officers, management employees and non-management exempt and non-exempt employees. Awards may be made in the form of incentive stock options, non-qualified stock options, stock appreciation rights, restricted stock or other stock based awards. The Company recognizes compensation expense in the financial statements only if the market price of the underlying stock exceeds the exercise price on the date of grant. The Company provides pro forma net income and pro forma earnings per share disclosures for employee stock option grants made in 1995 and future years based on the fair value of the options at the date of grant (see Note 9). Fair value of options granted is computed using the Black Scholes option pricing model.

**(l) Non Operating Gain on Subsidiary Stock and Minority Interest:**

On November 24, 1997, ELI completed an initial public offering (IPO) of 8,000,000 shares of its Class A Common Stock. The Company's policy is to account for sales of subsidiary stock as income statement transactions and as a result, in 1997, the Company recorded a pre-tax non operating gain of approximately \$78,700,000 resulting from this transaction and continues to consolidate ELI. The Company retained approximately 98% of the voting interest and approximately 83% of the economic ownership in ELI. Minority interest represents 17.35% of ELI's loss before income tax benefit and the cumulative effect of change in accounting principle as of December 31, 1998.

**(m) Net Income Per Common Share:**

Basic earnings per share (EPS) is computed using the weighted average number of common shares outstanding during the period being reported on. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock at the beginning of the period being reported on. Both Basic and Diluted EPS calculations are presented with adjustments for subsequent stock dividends. See Note 13 for reconciliation of basic EPS to diluted EPS.

**(n) Changes in Accounting Principles and New Accounting Pronouncements:**

In March 1998, the Accounting Standards Executive Committee of the AICPA released Statement of Position (SOP) 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." SOP 98-1 requires that certain costs for the development or purchase of internal-use software be capitalized and amortized over the estimated useful life of the software and costs for the preliminary project stage and the post-implementation/operations stage of an internal-use computer software development project be expensed as incurred. Capitalized software costs included in construction work in progress reflect costs for internally developed and purchased software. The impact of the early adoption of SOP 98-1 was to capitalize approximately \$6,100,000 in 1998 that would have been expensed had the Company not early adopted 98-1.

In April 1998, the Accounting Standards Executive Committee of the AICPA released Statement of Position (SOP) 98-5, "Reporting on the Costs of Start-Up Activities." SOP 98-5 requires that the unamortized portion of deferred start up costs be written off and reported as a change in accounting principle. Future costs of start-up activities should then be expensed as incurred. Certain third party direct costs incurred by ELI in connection with negotiating and securing initial rights-of-way and developing network design for new market clusters or locations had been capitalized by ELI in previous years and were being amortized over five years. The Company elected to early adopt SOP 98-5 effective January 1, 1998. The net book value of these deferred amounts was \$3,394,000 which has been reported as a cumulative effect of a change in accounting principle in the statement of income and comprehensive income for the year ended December 31, 1998, net of an income tax benefit of \$577,000 and the related minority interest of \$483,000.

In 1998, the Company adopted the provisions of SFAS No. 130 "Reporting Comprehensive Income." SFAS 130 establishes standards for reporting and presentation of comprehensive income and its components in a full set of financial statements. Comprehensive income for the Company consists of net income and net unrealized gains (losses) on available for sale securities and is presented in the consolidated statements of income and comprehensive income. The statement only requires additional disclosures in the consolidated financial statements; it does not affect the Company's financial position, cash flows or results of operations. Prior year financial statements have been conformed to satisfy the requirements of SFAS 130.

**Notes to Consolidated Financial Statements—(Continued)**

In 1998, the Company adopted the provisions SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information." SFAS 131 establishes standards for the way that public business enterprises report information about operating segments in annual financial statements and requires that those enterprises report selected information about operating segments in interim financial reports issued to shareholders. It also establishes standards for related disclosures about products and services, geographic areas and major customers. This Statement supersedes SFAS 14, "Financial Reporting for Segments of a Business Enterprise," but retains the requirement to report information about major customers. Segment information has been identified based on the way management organizes the segments within the Company for making operating decisions and assessing performance. Prior year information has been reclassified to conform with the current presentation.

In 1998, the Company adopted the provisions of SFAS 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits, an Amendment of FASB Statements No. 87, 88, and 106." SFAS 132 revises employers' disclosures about pension and other postretirement benefit plans. It does not change the measurement or recognition of those plans. SFAS 132 standardizes the disclosure requirements for pensions and other postretirement benefits to the extent practicable, requires additional information on changes in the benefit obligations and fair values of plan assets that will facilitate financial analysis, and eliminates certain disclosures that are no longer as useful as they were when SFAS 87, "Employers' Accounting for Pensions," SFAS 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits," and SFAS 106, "Employers' Accounting for Postretirement Benefits Other Than Pensions," were issued. Prior year disclosure has been restated to conform with the 1998 presentation.

**(2) Property, Plant and Equipment:**

The components of property, plant and equipment at December 31, 1998, 1997 and 1996 are as follows:

	1998	1997	1996
		(\$ in thousands)	
Transmission and distribution facilities.....	\$3,411,055	\$3,205,529	\$2,923,630
Production and generating facilities.....	1,202,847	1,103,720	960,422
Administrative facilities.....	679,862	429,254	368,178
Construction work in progress.....	478,731	411,708	187,692
Pumping, storage and purification facilities.....	135,552	132,404	122,340
Other.....	39,306	15,122	20,607
	<u>\$5,947,353</u>	<u>\$5,297,737</u>	<u>\$4,582,869</u>

**(3) Mergers and Acquisitions:**

In November 1998, the Company acquired all of the stock of Rhinelander Telecommunication, Inc. (RTI) for approximately \$84,000,000 in cash. RTI is a diversified telecommunications company engaged in providing local exchange, long distance, Internet access, wireless and cable television services to rural markets in Wisconsin. This transaction was accounted for using the purchase method of accounting and the results of operations of RTI have been included in the accompanying financial statements from the date of acquisition.

In October 1998, the Company acquired all of the stock of St. Charles Natural Gas Company for \$5,000,000 in cash. St. Charles Natural Gas Company is a natural gas distribution company serving 5,000 customers in Louisiana and will become part of the Company's Louisiana Gas Services operations. This transaction was accounted for using the purchase method of accounting and the results of operations of St. Charles Natural Gas Company have been included in the accompanying financial statements from the date of acquisition.

In December 1997, the Company acquired Ogden Telephone Company (Ogden) in a stock for stock transaction. In 1997 the Company issued 2,308,262 shares of Common Stock to effect the merger. In 1998, 288,554 additional shares of the Company's Common Stock were issued in connection with this transaction. Ogden was an independent telephone operating company providing services to residential and commercial customers in Monroe County, New York. This transaction was accounted for using the pooling of interests method of accounting and the results of operations of Ogden have been included in the accompanying financial statements since the beginning of the 1997 year. Prior year financial statements were not restated as the amounts were not significant.

**Notes to Consolidated Financial Statements—(Continued)**

In October 1997, the Company purchased the St. John The Baptist Parish Gas System in Louisiana, for approximately \$2,100,000 in cash. This system serves 2,200 customers. This transaction was accounted for using the purchase method of accounting and the results of operations of St. John The Baptist Parish Gas System have been included in the accompanying financial statements from the date of acquisition.

In October 1997, the Company purchased all of the outstanding stock of Gasco, Inc., now known as The Gas Company (TGC) for approximately \$100,000,000 in cash from BHP Hawaii. TGC is a gas distribution company serving approximately 66,000 customers throughout Hawaii. This transaction was accounted for using the purchase method of accounting and the results of operations of TGC have been included in the accompanying financial statements from the date of acquisition.

In December 1996, the Company acquired Conference-Call USA, Inc. (Conference-Call) in a stock for stock transaction. Conference-Call provides nationwide conference calling services and its subsidiary, Dial, Inc. (Dial), provides international dial-back services. The Company issued 1,289,133 shares of common stock in exchange for all of the common and preferred stock of Conference-Call. The agreement provides that Conference-Call and/or Dial would be required to issue additional shares if specified financial results are achieved in future periods. As a result, the Company issued 243,497 and 113,785 in 1998 and 1997, respectively, as part of this provision. This transaction was accounted for using the purchase method of accounting and the results of operations of Conference-Call have been included in the accompanying financial statements from the date of acquisition.

The following pro forma financial information presents the combined results of operations of the Company, RTI and TGC as if the acquisitions had occurred on January 1 of the year preceding the dates of acquisition. The pro forma financial information does not necessarily reflect the results of operations that would have occurred had the Company, RTI and TGC constituted a single entity during such periods. The effect of the other acquisitions discussed above would not significantly impact the pro forma results.

	1998	1997	1996
	(\$ in thousands, except for per share amounts)		
Revenues .....	\$1,560,000	\$1,488,000	\$1,396,000
Net income .....	\$ 56,000	\$ 13,000	\$ 184,000
Basic earnings per common share .....	\$ .22	\$ .05	\$ .70
Diluted earnings per common share .....	\$ .22	\$ .05	\$ .70

A subsidiary of the Company, in a joint venture with a subsidiary of Century Communications Corp. (Century), acquired and operates four cable television systems in southern California serving over 90,000 basic subscribers. Century is a cable television company of which Leonard Tow, the Chairman and Chief Executive Officer of the Company, is Chairman and Chief Executive Officer. In addition, Claire Tow, a Director of the Company, is a Senior Vice President and a Director of Century. A management board on which the Company and Century are equally represented governs the joint venture. A subsidiary of Century (the Manager) manages the day-to-day operations of the systems. The Manager does not receive a management fee but is reimbursed only for the actual costs it incurs on behalf of the joint venture. The Manager is obligated to pass through to the joint venture any discount, up to 5%, off the published prices of services or assets purchased for the joint venture for use in the systems. The Manager is entitled to retain any discount in excess of 5%. The Company accounts for the joint venture following the equity method of accounting. It is expected that these properties will become part of a larger partnership with Tele-Communications, Inc., a cable operator in California, and Century. Upon formation of the partnership, the Company will own 5.5% of this partnership, which will serve approximately 772,000 customers in the Los Angeles basin. In March 1999, Adelphia Communications Corporation (Adelphia) and Century announced the signing of a definitive agreement for the merger of Century with Adelphia (see Note 4). Upon consummation of the Adelphia/Century merger, the Company expects to sell to Adelphia its interest in the joint venture properties (or its interest in the partnership if the joint venture properties are transferred to the partnership before the Adelphia/Century merger).

**Notes to Consolidated Financial Statements—(Continued)****(4) Investments:**

The components of investments at December 31, 1998, 1997 and 1996 are as follows:

	<u>1998</u>	<u>1997</u>	<u>1996</u>
		(\$ in thousands)	
State and municipal securities .....	\$141,202	\$212,743	\$370,783
Centennial Preferred Security .....	107,679	107,679	107,679
Marketable equity securities .....	163,661	75,855	58,351
Other fixed income securities .....	<u>2,219</u>	<u>2,222</u>	<u>2,339</u>
Total .....	<u>\$414,761</u>	<u>\$398,499</u>	<u>\$539,152</u>

Marketable equity securities for 1998, 1997 and 1996 include the Company's investments in Hungarian Telephone and Cable Corp. (HTCC), Centennial Class B Common Stock and Century Class A Common Stock. The investment in the shares of Century Class A Common Stock represents approximately 2% of the total outstanding common stock of Century and was recorded at a market value of approximately \$31¾ per share as of December 31, 1998. The Chairman and Chief Executive Officer of the Company is also Chairman and Chief Executive Officer of Century. Centennial was a subsidiary of Century. There were no sales of marketable equity securities in 1998, 1997 or 1996. The Company recognized \$22,138,000 in Other income (loss), net in 1996 for guarantees and financial support provided by the Company to HTCC.

In March 1999, Adelphia Communications Corporation and Century Communications Corp. announced the signing of a definitive agreement for the merger of Century with Adelphia. The Company currently owns 1,807,095 shares of Century Class A Common Stock. Pursuant to the Merger Agreement, each Century Class A Common share will be exchanged for cash of \$9.16 and .6122 of a share of Adelphia Class A Common Stock (for a total market value of \$44.14 per Century Class A Common share based on Adelphia's March 4, 1999 closing price of \$57⅞).

The following summarizes the amortized cost, gross unrealized holding gains and losses and fair market value for investments.

<u>Investment Classification</u>	<u>Amortized Cost</u>	<u>Unrealized Holding</u>		<u>Aggregate Fair</u>
		<u>Gains</u>	<u>(Losses)</u>	
		(\$ in thousands)		
<u>As of December 31, 1998</u>				
Held-To-Maturity .....	\$107,679	\$ 15,673	\$ —	\$123,352
Available-For-Sale .....	215,228	100,329	(8,475)	307,082
<u>As of December 31, 1997</u>				
Held-To-Maturity .....	\$107,679	\$ 78,608	\$ —	\$186,287
Available-For-Sale .....	284,630	19,673	(13,483)	290,820
<u>As of December 31, 1996</u>				
Held-To-Maturity .....	\$107,679	\$ 78,608	\$ —	\$186,287
Available-For-Sale .....	442,834	2,903	(14,264)	431,473

The amortized cost of held-to-maturity securities plus the aggregate fair market value of available-for-sale securities for each year presented above equals the total of investments presented in the foregoing investments table. As of December 31, 1998, all investments except the Centennial Preferred Security have been classified as available-for-sale. The fair market value of the Centennial Preferred Security was estimated to be its accreted value at December 31, 1997 and 1996 and its conversion value at December 31, 1998. The fair market value reflected above for the Centennial Preferred Security and Class B Common Stock at December 31, 1998 approximates the amount the Company realized in January 1999 (see Note 1(i)).

In 1995, the Company made an investment in and entered into definitive agreements with HTCC. In 1997, the Company acquired additional shares in the open market. Pursuant to a definitive agreement, the Company had been providing requested management services to HTCC. Expenses incurred by the Company in providing such services, including allocable overhead items, were required to be reimbursed by HTCC. HTCC disputed certain provisions of this definitive agreement and the associated management fee. In September 1998, HTCC satisfied

**Notes to Consolidated Financial Statements—(Continued)**

its current obligations with the Company by issuing to the Company 100,000 shares of its common stock and an \$8,400,000 note, dated September 30, 1998, bearing interest payable annually at the rate of LIBOR (for one-year dollar deposits) plus 2.5%, maturing in 2004. No gain or loss was recognized on this transaction. Additionally, the current management services agreement was terminated and a new seven-year consulting services agreement between the Company and HTCC was entered into with services to begin in 2004. HTCC has agreed to pay the Company a combined termination/consulting fee in the aggregate amount of \$21,000,000 in equal annual installments of \$3,000,000 beginning in 2004.

The investment in HTCC declined in value during 1998 and in the fourth quarter of 1998 management determined that the decline was other than temporary. As a result, the Company recognized a loss of \$31,900,000 in the HTCC investment as a reduction of Other income (loss), net in the statement of income and comprehensive income.

**(5) Fair Value of Financial Instruments:**

The following table summarizes the carrying amounts and estimated fair values for certain of the Company's financial instruments at December 31, 1998, 1997 and 1996. For the other financial instruments, representing cash, accounts and notes receivables, short-term debt, accounts payable and other accrued liabilities, the carrying amounts approximate fair value due to the relatively short maturities of those instruments.

	1998		1997		1996	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value	Carrying Amount	Fair Value
	(\$ in thousands)					
Investments .....	\$ 414,761	\$ 430,434	\$ 398,499	\$ 477,107	\$ 539,152	\$ 617,760
Long-term debt ...	1,900,246	2,008,422	1,706,532	1,786,622	1,509,697	1,532,251
EPPICS .....	201,250	171,566	201,250	192,194	201,250	192,194

The fair value of the above financial instruments, except for the investment in the Centennial Preferred Security, are based on quoted prices at the reporting date for those financial instruments. The fair value of the Centennial Preferred Security was estimated to be its accreted value at December 1997 and 1996 and its conversion value at December 31, 1998 (based on its conversion as a result of the merger with CCW Acquisition Corporation discussed in Note 1(i)).

**(6) Long-term Debt:**

	Weighted average interest rate at December 31, 1998	Maturities	December 31,		
			1998	1997	1996
	(\$ in thousands)				
Debentures .....	7.34%	2001-2046	\$1,000,000	\$1,000,000	\$1,000,000
Industrial development revenue bonds .....	4.95%	2015-2033	458,417	439,277	391,789
ELI bank credit facility .....	5.61%	2002	284,000	60,000	—
Rural Utilities Service Loan Contracts .....	5.85%	2000-2027	91,078	87,053	77,909
Senior unsecured notes .....	8.05%	2012	36,000	36,000	36,000
Other long-term debt .....	7.37%	1999-2027	30,751	16,202	3,999
Commercial paper notes payable ...			—	68,000	—
Total long-term debt .....			<u>\$1,900,246</u>	<u>\$1,706,532</u>	<u>\$1,509,697</u>

The total principal amounts of industrial development revenue bonds at December 31, 1998, 1997 and 1996 were \$500,195,000, \$480,195,000 and \$422,780,000, respectively. Funds from industrial development revenue bond issuances are held by a trustee until qualifying construction expenditures are made at which time the funds are released. The amounts presented in the table above represent funds that have been used for construction through December 31, 1998, 1997 and 1996, respectively.

**Notes to Consolidated Financial Statements—(Continued)**

On December 31, 1997, certain commercial paper notes payable were classified as long-term debt because the obligations were refinanced with long-term debt securities.

The Company has available lines of credit with commercial banks in the amounts of \$375,000,000 and \$200,000,000, which expire on December 8, 1999 and December 16, 2003, respectively, and have associated facility fees of one-thirty third of one percent (.03%) per annum and one twentieth of one percent (.05%) per annum, respectively. The terms of the lines of credit provide the Company with extension options. No amounts are outstanding under these facilities. ELI, a subsidiary of the Company, has committed lines of credit with commercial banks under which it may borrow up to \$400,000,000 which is guaranteed by the Company and expire November 21, 2002. The ELI credit facility has an associated facility fee of one-twentieth of one percent (.05%) per annum. There is \$284,000,000 outstanding under these facilities.

The installment principal payments and maturities of long-term debt for the next five years are as follows:

	1999	2000	2001	2002	2003
	(\$ in thousands)				
Installment principal payments .....	\$8,930	\$6,990	\$ 5,490	\$ 5,524	\$5,971
Maturities .....	—	—	50,000	284,000	—
	<u>\$8,930</u>	<u>\$6,990</u>	<u>\$55,490</u>	<u>\$289,524</u>	<u>\$5,971</u>

Holders of certain industrial development revenue bonds may tender at par prior to maturity. The next tender date is April 1, 2001 for \$14,400,000 of principal amount of bonds. The Company expects to remarket all such bonds which are tendered. In the years 1998, 1997 and 1996, interest payments on short- and long-term debt were \$123,107,000, \$112,127,000 and \$93,274,000, respectively.

**(7) Company Obligated Mandatorily Redeemable Convertible Preferred Securities:**

During the first quarter of 1996, a consolidated wholly-owned subsidiary of the Company, Citizens Utilities Trust (the Trust), issued, in an underwritten public offering, 4,025,000 shares of 5% Company Obligated Mandatorily Redeemable Convertible Preferred Securities due 2036 (Trust Convertible Preferred Securities or EPPICS), representing preferred undivided interests in the assets of the Trust, with a liquidation preference of \$50 per security (for a total liquidation amount of \$201,250,000). The proceeds from the issuance of the Trust Convertible Preferred Securities and a Company capital contribution were used to purchase \$207,475,000 aggregate liquidation amount of 5% Partnership Convertible Preferred Securities due 2036 from another wholly owned consolidated subsidiary, Citizens Utilities Capital L.P. (the Partnership). The proceeds from the issuance of the Partnership Convertible Preferred Securities and a Company capital contribution were used to purchase from the Company \$211,756,050 aggregate principal amount of 5% Convertible Subordinated Debentures Due 2036. The sole assets of the Trust are the Partnership Convertible Preferred Securities, and the Company's Convertible Subordinated Debentures are substantially all the assets of the Partnership. The Company's obligations under the agreements related to the issuances of such securities, taken together, constitute a full and unconditional guarantee by the Company of the Trust's obligations relating to the Trust Convertible Preferred Securities and the Partnership's obligations relating to the Partnership Convertible Preferred Securities. The \$196,722,000 of net proceeds from the issuances was used to permanently fund a portion of the acquisition of telecommunications properties.

In accordance with the terms of the issuances, the Company paid the 5% interest on the Convertible Subordinated Debentures in Citizens' Common Stock. During 1998, 1,093,274 shares of Common Stock were issued to the Partnership in payment of interest of which 1,009,231 shares were sold by the Partnership to satisfy cash dividend payment elections by the holders of the EPPICS. The sales proceeds and the remaining 84,043 shares of Common Stock were distributed by the Partnership to the Trust. During 1997, 986,579 shares of Common Stock were issued to the Partnership in payment of interest of which 952,007 shares were sold by the Partnership to satisfy cash dividend payment elections by the holders of the EPPICS. The sales proceeds and the remaining 34,572 shares of Common Stock were distributed by the Partnership to the Trust. During 1996, 709,748 shares of Common Stock Series A were issued to the Partnership in payment of interest of which 654,119 shares were sold by the Partnership to satisfy cash dividend payment elections by the holders of the EPPICS. The sales proceeds and the remaining 55,629 shares of Common Stock Series A were distributed by the Partnership to the Trust. The Trust distributed the cash and shares as dividends to the holders of the EPPICS in 1998, 1997 and 1996.

**Notes to Consolidated Financial Statements—(Continued)****(8) Capital Stock:**

The common stock of the Company had consisted of two series, Series A and Series B. On August 25, 1997, the Board of Directors voted to convert the shares of Series A Common Stock into Series B Common Stock at a ratio of one share of Series B Common Stock for each share of Series A Common Stock. The result of this conversion was one class of stock now referred to as the Common Stock. The 1997 and 1996 consolidated financial statements give retroactive effect to the aforementioned conversion. The Company is authorized to issue up to 600,000,000 shares of Common Stock. Quarterly stock dividends had been declared and issued on Common Stock and shareholders had the option of enrolling in the "Common Stock Dividend Sale Plan." The plan offered shareholders the opportunity to have their stock dividends sold by the plan broker and the net cash proceeds of the sale distributed to them quarterly.

The amount and timing of dividends payable on Common Stock are within the sole discretion of the Company's Board of Directors. The Board of Directors has undertaken an extensive review of the Company's dividend policy in conjunction with its separation plans. Resulting from this review, in November 1998, the Board of Directors concluded that after the payment of the December 1998 stock dividend, the Company should discontinue the payment of stock dividends at least through the separation. Post-separation dividend policies for both the new company and Citizens Utilities Company will continue to be evaluated and will be subject to approval by each company's board of directors. In 1998, 1997 and 1996, the Board of Directors reviewed alternative stock dividend cash equivalents and associated stock dividend rates each quarter in order to determine and declare a prudent stock dividend rate in light of the Company's actual and forecasted financial position and results of operations, as well as dividend yields of comparable communications and public services companies.

Quarterly and annual stock dividend rates declared and annual stock dividend cash equivalents (adjusted for all stock dividends paid subsequent to all dividends declared through December 31, 1998, and rounded to the nearest  $\frac{1}{16}^{\text{th}}$ ) considered by the Board have been as follows:

	Dividend Rates		
	1998	1997	1996
First quarter .....	.75%	1.6%	1.6%
Second quarter.....	.75%	1.6%	1.6%
Third quarter .....	.75%	1.0%	1.6%
Fourth quarter.....	.75%	1.0%	1.6%
Total.....	<u>3.0%</u>	<u>5.2%</u>	<u>6.4%</u>
Compounded Total.....	<u>3.03%</u>	<u>5.30%</u>	<u>6.56%</u>
Cash Equivalent .....	<u>28<math>\frac{1}{16}</math>¢</u>	<u>51<math>\frac{1}{4}</math>¢</u>	<u>66<math>\frac{1}{8}</math>¢</u>

The Company purchased 1,811,000 shares at a cost of \$14,826,000 in 1998, 4,904,000 shares at a cost of \$48,552,000 in 1997, and 6,554,000 shares at a cost of \$75,481,000 in 1996. All purchased shares were used to pay stock dividends.

**Notes to Consolidated Financial Statements—(Continued)**

The activity in shares of outstanding common stock during 1998, 1997 and 1996 is summarized as follows:

	<u>Number of Shares</u>
Balance at January 1, 1996.....	227,587,000
Acquisition .....	1,289,000
Common stock dividends .....	14,803,000
Common stock buybacks to fund stock dividends.....	(6,554,000)
Common stock issued to fund EPPICS dividends.....	710,000
Stock plans.....	<u>1,313,000</u>
Balance at December 31, 1996.....	239,148,000
Acquisition .....	2,417,000
Common stock dividends .....	12,591,000
Common stock buybacks to fund stock dividends.....	(4,904,000)
Common stock issued to fund EPPICS dividends.....	986,000
Stock plans.....	<u>756,000</u>
Balance at December 31, 1997.....	250,994,000
Acquisitions .....	532,000
Common stock dividends.....	7,657,000
Common stock buybacks to fund stock dividends.....	(1,811,000)
Common stock issued to fund EPPICS dividends.....	1,093,000
Stock plans.....	<u>684,000</u>
Balance at December 31, 1998.....	<u><u>259,149,000</u></u>

The Company has 50,000,000 authorized but unissued shares of preferred stock (\$.01 par).

**(9) Stock Plans:**

At December 31, 1998, the Company had four stock based compensation plans and ELI had two stock based plans which are described below. The Company applies APB Opinion No. 25 and related interpretations in accounting for the employee stock plans. No compensation cost has been recognized in the financial statements for options issued pursuant to the Management Equity Incentive Plan (MEIP), Equity Incentive Plan (EIP), Employee Stock Purchase Plan (ESPP), ELI Employee Stock Purchase Plan (ELI ESPP) or ELI Equity Incentive Plan (ELI EIP) as the exercise price for such options was equal to the market price of the stock at the time of grant. Compensation cost recognized for the Company's Directors' Deferred Fee Equity Plan was \$463,798, \$352,017 and \$161,231 in 1998, 1997 and 1996, respectively. Had the Company determined compensation cost based on the fair value at the grant date for its MEIP, EIP, ESPP, ELI ESPP and ELI EIP, the Company's pro forma Net income and Net income per share would have been as follows:

		<u>1998</u>	<u>1997</u>	<u>1996</u>
			(\$ in thousands)	
Net Income	As reported	\$57,060	\$10,100	\$178,660
	Pro forma	45,409	7,374	176,662
Net Income per common share	As reported:			
	Basic	\$ .22	\$ .04	\$ .68
	Diluted	.22	.04	.68
	Pro forma:			
	Basic	\$ .18	\$ .03	\$ .68
	Diluted	.17	.03	.67

Pro forma Net income reflects only the vested portion of options granted in 1998, 1997, 1996 and 1995. Therefore, the full impact of calculating compensation cost for stock options is not reflected in the pro forma amounts above because pro forma compensation cost only includes costs associated with the vested portion of options granted pursuant to the MEIP, EIP, ESPP, ELI ESPP and ELI EIP on or after January 1, 1995.

**Notes to Consolidated Financial Statements—(Continued)**

In November 1998, the Compensation Committee of the Company's Board of Directors approved a stock option exchange program pursuant to which current employees of the Company (excluding senior executive officers) holding outstanding options, under the MEIP and EIP plans, with an exercise price in excess of \$10.00 had the right to exchange their options for a lesser number of new options with an exercise price of \$7.75. A calculation was prepared using the Black Scholes option pricing model to determine the exchange rate for each eligible grant in order to keep the fair value of options exchanged equal to the fair value of the options reissued. The exchanged options maintain the same vesting and expiration terms. This stock option exchange program had no impact on reported earnings and resulted in an aggregate net reduction in shares subject to option of 2,202,000 for both MEIP and EIP.

In August 1998, the Compensation Committee of ELI's Board of Directors approved a stock option exchange program pursuant to which employees of ELI holding outstanding options with an exercise price in excess of \$15.50 had the right to exchange all or half of their options for a lesser number of new options with an exercise price of \$8.75. A calculation was prepared using the Black Scholes option pricing model to determine the exchange rate for each eligible grant in order to keep the fair value of options exchanged equal to the fair value of the options reissued. The repriced options maintain the same vesting and expiration terms. This stock option exchange program had no impact on reported earnings and resulted in a net reduction in shares subject to option of 546,000.

Both ELI and the Company repriced these employee stock options in an effort to retain employees at a time when a significant percentage of employee stock options had exercise prices that were above fair market value. No compensation costs have been recognized in the financial statements as the exercise price was equal to the market value of the stock at the date of repricing.

**Management Equity Incentive Plan**

Under the MEIP, awards of the Company's Common Stock may be granted to eligible officers, management employees and non-management exempt employees of the Company and its subsidiaries in the form of incentive stock options, non-qualified stock options, stock appreciation rights (SARs), restricted stock or other stock-based awards. The MEIP is administered by the Compensation Committee of the Board of Directors.

The maximum number of shares of common stock which may be issued pursuant to awards at any time is 5% (12,957,000 as of December 31, 1998) of the Company's common stock outstanding. No awards will be granted more than 10 years after the effective date (June 22, 1990) of the MEIP. The exercise price of stock options and SARs shall be equal to or greater than the fair market value of the underlying common stock on the date of grant. Stock options are generally not exercisable on the date of grant but vest over a period of time.

Under the terms of the MEIP, subsequent stock dividends and stock splits have the effect of increasing the option shares outstanding, which correspondingly decreases the average exercise price of outstanding options.

**Notes to Consolidated Financial Statements—(Continued)**

The following is a summary of share activity subject to option under the MEIP adjusted for subsequent stock dividends.

	Shares Subject to Option	Weighted Average Option Price Per Share
Balance at January 1, 1996 .....	8,714,000	\$12.37
Options granted .....	3,084,000	10.54
Options exercised .....	(392,000)	6.66
Options canceled or lapsed .....	(606,000)	11.23
Balance at December 31, 1996 .....	10,800,000	11.02
Options granted .....	1,641,000	8.53
Options exercised .....	(106,000)	10.81
Options canceled or lapsed .....	(631,000)	11.03
Balance at December 31, 1997 .....	11,704,000	10.72
Options granted .....	1,869,000	7.75
Options exercised .....	(29,000)	10.56
Options canceled, forfeited or lapsed .....	(4,109,000)	11.09
Balance at December 31, 1998 .....	<u>9,435,000</u>	\$ 9.91

As a result of the stock option exchange program approved by the Compensation Committee of the Board of Directors, a total of 3,801,000 options were eligible for exchange, of which 3,554,000 options were canceled in exchange for 1,869,000 new options with an exercise price of \$7.75.

The following table summarizes information about shares subject to options under the MEIP at December 31, 1998.

Options Outstanding				Options Exercisable	
Number Outstanding	Range of Exercise Prices	Weighted Average Exercise Price	Weighted Average Remaining Life in Years	Number Exercisable	Weighted Average Exercise Price
14,000	\$ 4 – 5	\$ 4	6	14,000	\$ 4
2,615,000	7 – 8	8	5	1,960,000	8
1,636,000	8 – 10	9	9	617,000	9
2,264,000	10 – 11	11	6	1,678,000	11
2,343,000	11 – 14	12	4	2,338,000	12
563,000	14 – 15	14	5	563,000	14
<u>9,435,000</u>	\$ 4 – 15	\$10	6	<u>7,170,000</u>	\$10

The weighted average fair value of options granted during 1998, 1997 and 1996 were \$2.27, \$4.23 and \$4.61, respectively. For purposes of the pro forma calculation, the fair value of each option grant is estimated on the date of grant using the Black Scholes option pricing model with the following weighted average assumptions used for grants in 1998, 1997 and 1996:

	1998	1997	1996
Dividend yield .....	—	—	—
Expected volatility .....	26%	32%	20%
Risk-free interest rate .....	4.43%	6.13%	5.63%
Expected life .....	4 years	7 years	7 years

During 1996, the Company granted 566,694 shares (adjusted for subsequent stock dividends) of restricted stock awards to key employees in the form of the Company's Common Stock. None of the restricted stock may be sold, assigned, pledged or otherwise transferred, voluntarily or involuntarily, by the employees until the restrictions lapse in January 2001. At December 31, 1998, 559,974 shares (adjusted for subsequent stock dividends) of restricted stock were outstanding.

**Notes to Consolidated Financial Statements—(Continued)**

Compensation expense of \$1,288,000, \$1,302,000 and \$1,125,000 for the years ended December 31, 1998, 1997 and 1996, respectively, has been recorded in connection with these grants.

**Equity Incentive Plan**

In May 1996, the shareholders of the Company approved the EIP. Under the EIP, awards of the Company's Common Stock may be granted to eligible officers, management employees and non-management employees of the Company and its subsidiaries in the form of incentive stock options, non-qualified stock options, stock appreciation rights (SARs), restricted stock or other stock-based awards. The EIP is administered by the Compensation Committee of the Board of Directors.

The maximum number of shares of common stock which may be issued pursuant to awards at any time is 12,858,000 shares, which has been adjusted for subsequent stock dividends. No awards will be granted more than 10 years after the effective date (May 23, 1996) of the EIP. The exercise price of stock options and SARs shall be equal to or greater than the fair market value of the underlying common stock on the date of grant. Stock options are generally not exercisable on the date of grant but vest over a period of time.

Under the terms of the EIP, subsequent stock dividends and stock splits have the effect of increasing the option shares outstanding, which correspondingly decrease the average exercise price of outstanding options.

The following is a summary of share activity subject to option under the EIP adjusted for subsequent stock dividends.

	Shares Subject to Option	Weighted Average Option Price Per Share
Balance at January 1, 1997.....	—	\$ —
Options granted.....	2,197,000	8.55
Options canceled or lapsed.....	<u>(3,000)</u>	8.53
Balance at December 31, 1997.....	2,194,000	8.55
Options granted.....	4,683,000	9.34
Options canceled, forfeited or lapsed .....	<u>(2,745,000)</u>	10.14
Balance at December 31, 1998.....	<u>4,132,000</u>	\$ 8.51

As a result of the stock option exchange program approved by the Compensation Committee of the Board of Directors, a total of 2,453,000 options were eligible for exchange, of which 2,123,000 options were canceled in exchange for 1,606,000 new options with an exercise price of \$7.75.

The following table summarizes information about shares subject to options under the EIP at December 31, 1998.

Options Outstanding				Options Exercisable	
Number Outstanding	Range of Exercise Prices	Weighted Average Exercise Price	Weighted Average Remaining Life in Years	Number Exercisable	Weighted Average Exercise Price
1,602,000	\$ 7 – 8	\$ 8	9	5,000	\$ 8
1,758,000	8 – 9	9	9	617,000	9
171,000	9 – 10	9	9	3,000	9
<u>601,000</u>	10 – 11	10	9	<u>22,000</u>	10
<u>4,132,000</u>	\$ 7 – 11	\$ 9	9	<u>647,000</u>	\$ 9

**Notes to Consolidated Financial Statements—(Continued)**

The weighted average fair value of options granted during 1998 and 1997 was \$3.54 and \$4.25, respectively. For purposes of the pro forma calculation, the fair value of each option grant is estimated on the date of grant using the Black Scholes option pricing model with the following weighted average assumptions used for grants in 1998 and 1997:

	<u>1998</u>	<u>1997</u>
Dividend yield .....	—	—
Expected volatility .....	26%	32%
Risk-free interest rate .....	5.15%	6.14%
Expected life .....	6 years	7 years

During 1998 and 1997, the Company granted restricted stock awards to key employees in the form of the Company's Common Stock. The number of shares issued as restricted stock awards during 1998 and 1997 were 464,409 and 23,018, respectively (adjusted for subsequent stock dividends). The 1998 awards were issued to retain certain key employees. None of the restricted stock awards may be sold, assigned, pledged or otherwise transferred, voluntarily or involuntarily, by the employees until the restrictions lapse. The restrictions are both time and performance based. At December 31, 1998, 487,428 shares (adjusted for subsequent stock dividends) of restricted stock were outstanding.

Compensation expense of \$808,000 and \$27,000 for the years ended December 31, 1998 and 1997, respectively, has been recorded in connection with these grants.

**Employee Stock Purchase Plan**

The Company's ESPP was approved by shareholders on June 12, 1992 and amended on May 22, 1997. Under the ESPP, eligible employees of the Company and its subsidiaries have the right to subscribe to purchase shares of Common Stock at the lesser of 85% of the mean between the high and low market prices on the first day of the purchase period or on the last day of the purchase period. An employee may elect to have up to 20% of annual base pay withheld in equal installments throughout the designated payroll-deduction period for the purchase of shares. The value of an employee's subscription may not exceed \$25,000 in any one calendar year. An employee may not participate in the ESPP if such employee owns stock possessing 5% or more of the total combined voting power or value of the Company's capital stock. As of December 31, 1998, there were 6,407,195 shares of Common Stock reserved for issuance under the ESPP. These shares may be adjusted for any future stock dividends or stock splits. The ESPP will terminate when all shares reserved have been subscribed for and purchased, unless terminated earlier or extended by the Board of Directors. The ESPP is administered by the 1992 Employee Stock Purchase Plan Committee of the Board of Directors. As of December 31, 1998, the number of employees enrolled and participating in the ESPP was 1,986 and the total number of shares purchased under the ESPP was 2,604,912. For purposes of the pro forma calculation, compensation cost is recognized for the fair value of the employees' purchase rights, which was estimated using the Black Scholes option pricing model with the following assumptions for subscription periods beginning in 1998, 1997 and 1996:

	<u>1998</u>	<u>1997</u>	<u>1996</u>
Dividend yield .....	—	—	—
Expected volatility .....	26%	32%	20%
Risk-free interest rate .....	4.91%	5.45%	5.29%
Expected life .....	6 months	6 months	6 months

The weighted average fair value of those purchase rights granted in 1998, 1997 and 1996 was \$3.66, \$3.04 and \$3.47, respectively.

**ELI Employee Stock Purchase Plan**

The ELI ESPP was approved by shareholders on May 21, 1998. Under the ELI ESPP, eligible employees of ELI may subscribe to purchase shares of ELI Class A Common Stock at the lesser of 85% of the average of the high and low market prices on the first day of the purchase period or on the last day of the purchase period. An employee may elect to have up to 20% of annual base pay withheld in equal installments throughout the designated payroll-deduction period for the purchase of shares. The value of an employee's subscription may not exceed \$25,000 in any one calendar year. An employee may not participate in the ELI ESPP if such employee owns stock possessing

**Notes to Consolidated Financial Statements—(Continued)**

5% or more of the total combined voting power or value of all classes of capital stock of ELI. As of December 31, 1998, there were 200,000 shares of ELI Class A Common Stock reserved for issuance under the ELI ESPP. These shares may be adjusted for any future stock dividends or stock splits. The ESPP will terminate when all shares reserved have been subscribed for and purchased, unless terminated earlier or extended by the Board of Directors. The ELI ESPP is administered by the Compensation Committee of ELI's Board of Directors. As of December 31, 1998, the number of employees enrolled and participating in the ELI ESPP was 468 and the total number of shares purchased under the ELI ESPP was 119,345. For purposes of the pro forma calculation, compensation cost is recognized for the fair value of the employees' purchase rights, which was estimated using the Black Scholes option pricing model with the following assumptions for subscription periods beginning in 1998:

	<u>1998</u>
Dividend yield .....	—
Expected volatility .....	71%
Risk-free interest rate .....	4.92%
Expected life .....	6 months

The weighted average fair value of those purchase rights granted in 1998 was \$3.82.

**ELI Equity Incentive Plan**

In October 1997, the Board of Directors of ELI approved the ELI EIP. Under the ELI EIP, awards of ELI's Class A Common Stock may be granted to eligible directors, officers, management employees, non-management employees and consultants of ELI in the form of incentive stock options, non-qualified stock options, SARs, restricted stock or other stock-based awards. The ELI EIP is administered by the Compensation Committee of the ELI Board of Directors. The exercise price for such awards shall not be less than 85% or more than 110% of the average of the high and low stock prices on the date of grant. The exercise period for such awards is generally 10 years from the date of grant. ELI has reserved 4,170,600 shares for issuance under the terms of this plan.

The following is a summary of share activity subject to option under the ELI EIP.

	Shares Subject to Option	Weighted Average Option Price Per Share
Balance at January 1, 1997.....	—	\$ —
Options granted .....	<u>2,326,000</u>	16.00
Balance at December 31, 1997.....	2,326,000	16.00
Options granted .....	1,654,000	10.77
Options canceled, forfeited or lapsed .....	<u>(1,649,000)</u>	16.21
Balance at December 31, 1998 .....	<u>2,331,000</u>	\$12.14

As a result of the stock option exchange program approved by the ELI Compensation Committee of the Board of Directors, a total of 2,212,000 options were eligible for exchange, of which 1,426,000 options were canceled in exchange for 880,000 new options.

**Notes to Consolidated Financial Statements—(Continued)**

The following table summarizes information about shares subject to options under the EIP at December 31, 1998.

Options Outstanding				Options Exercisable	
Number Outstanding	Range of Exercise Prices	Weighted Average Exercise Price	Weighted Average Remaining Life in Years	Number Exercisable	Weighted Average Exercise Price
1,261,000	\$ 8 – 9	\$ 9	9	268,000	\$ 9
32,000	9 – 16	13	9	27,000	13
963,000	16 – 17	16	9	320,000	16
75,000	17 – 20	19	9	—	—
<u>2,331,000</u>	\$ 8 – 20	\$12	9	<u>615,000</u>	\$13

For purposes of the pro forma calculation, compensation cost is recognized for the fair value of the employees' purchase rights, which was estimated using the Black Scholes option pricing model with the following assumptions for subscription periods beginning in 1998 and 1997:

	1998	1997
Dividend yield .....	—	—
Expected volatility .....	71%	13%
Risk-free interest rate .....	5.44%	5.87%
Expected life .....	6 years	7 years

The weighted-average fair value of those options granted in 1998 and 1997 were \$6.94 and \$5.13, respectively.

In conjunction with the IPO, ELI granted 535,000 restricted stock awards to key employees in the form of Class A Common Stock. Subsequently in 1997, 15,000 shares were returned and canceled. None of the restricted stock awards may be sold, assigned, pledged or otherwise transferred, voluntarily or involuntarily, by the employee until the restrictions lapse. For 395,000 shares, restrictions lapse over one through three-year periods, including one-third of the shares when ELI achieves \$100,000,000 of annual revenues, one-third of the shares when ELI achieves \$125,000,000 of annual revenues, and one-third of the shares when ELI achieves \$155,000,000 of annual revenues. For the remaining 125,000 shares, restrictions will lapse in January 2001 if certain performance targets are met. At December 31, 1998, 520,000 shares of this stock were outstanding, of which 131,667 shares were no longer restricted pending board approval. Compensation expense of \$4,666,000 and \$219,000 for the years ended December 31, 1998 and 1997, respectively, has been recorded in connection with this grant.

**Directors' Deferred Fee Equity Plan**

The Company's Non-Employee Directors' Deferred Fee Equity Plan (the Directors' Plan) was approved by shareholders on May 19, 1995 and subsequently amended. The Directors' Plan includes an Option Plan, a Stock Plan and a Formula Plan. Through the Option Plan, an eligible director may elect to receive up to \$30,000 per annum of his or her director's fees for a period of up to five years in the form of options to purchase Company common stock, the number of such options being equal to such fees divided by 20% of the fair market value of Company common stock on the effective date of the options and are exercisable at 90% of the fair market value of Company common stock on the effective date of the options. Through the Stock Plan, an eligible director may elect to receive all or a portion of his or her director's fees in the form of Plan Units, the number of such Plan Units being equal to such fees divided by the fair market value of Company common stock on certain specified dates. The Formula Plan provides each Director of the Company options to purchase 5,000 shares of common stock on the first day of each year beginning in 1997 and continuing through 2002 regardless of whether the Director is participating in the Option Plan or Stock Plan. In addition, on September 1, 1996, options to purchase 2,500 shares of common stock were granted to each Director. The exercise price of the options are 100% of the fair market value on the date of grant and the options are exercisable six months after the grant date and remain exercisable for ten years after the grant date. In the event of termination of Directorship, a Stock Plan participant will receive the value of such Plan Units in either stock or cash or installments of cash as selected by the Participant at the time of the related Stock Plan election. As of any date, the maximum number of shares of common stock which the Plan may be obligated to deliver pursuant to the Stock Plan and the maximum number of shares of

**Notes to Consolidated Financial Statements—(Continued)**

common stock which shall have been purchased by Participants pursuant to the Option Plan and which may be issued pursuant to outstanding options under the Option Plan shall not be more than one percent (1%) of the total outstanding shares of Common Stock of the Company as of such date, subject to adjustment in the event of changes in the corporate structure of the Company affecting capital stock. There were 11 directors participating in the Directors' Plan in 1998. In 1998, the total Options and Plan Units earned were 185,090 and 16,661, respectively (adjusted for subsequent stock dividends). In 1997, the total Options and Plan Units earned were 188,838 and 18,817, respectively (adjusted for subsequent stock dividends). In 1996, the total Options and Plan Units earned were 160,151 and 15,585, respectively (adjusted for subsequent stock dividends). At December 31, 1998, 525,422 options were exercisable at a weighted average exercise price of \$9.98.

**(10) 1997 Charges to Earnings:**

In 1996 and early 1997, the Company had been pursuing an aggressive growth strategy to take advantage of opportunities in the emerging communications marketplace. This strategy included the initiation and expansion of long distance services which, in combination with other enhanced service offerings, would enable the Company to offer an integrated package of products and services.

Late in 1996, the Company began the transition of its long distance network, primarily to fixed cost leases, in order to achieve the lowest cost of providing long distance service. In addition, the Company initiated a brand recognition program to support the sales and marketing initiatives designed to increase the Company's market share. The increase in revenues resulting from this growth strategy, though significant, did not offset the resulting increase in incremental expenses from the branding, sales, and marketing initiatives. As a result, the Company's long distance service operations generated unexpected losses during the first half of 1997 which had an adverse impact on the Company's earnings and cash flow. During the second quarter 1997, management re-evaluated this growth strategy in light of this continuing impact on earnings and cash flow.

In connection with the re-evaluation of the Company's communications growth strategy, as well as a review of its employee benefit plans to determine if such plans were competitive with those provided in the industry, several public utility commission orders requiring the Company to record charges to earnings, and other charges to earnings related to certain accounting policy changes at ELI in anticipation of its initial public offering, the Company recorded approximately \$197,300,000 of charges to earnings in 1997 as follows:

	<u>1997</u>
	(\$ in thousands)
Curtailment of certain long distance service operations .....	\$ 34,600
Benefit plan curtailments and related regulatory assets .....	34,700
Telecommunications information systems and software .....	67,400
Regulatory commission orders .....	47,200
Other .....	13,400
Total .....	<u>\$197,300</u>

**(11) Income Taxes:**

The following is a reconciliation of the provision for income taxes at federal statutory rates to the effective rates.

	<u>1998</u>	<u>1997</u>	<u>1996</u>
Consolidated tax provision at federal statutory rate .....	35.0%	35.0%	35.0%
State income tax provisions, net of federal income tax benefit .....	1.3%	8.6%	0.5%
Allowance for funds used during construction .....	(2.7%)	(4.2%)	(2.0%)
Nontaxable investment income .....	(3.3%)	(19.9%)	(1.7%)
Amortization of investment tax credits .....	(1.9%)	(7.3%)	(0.7%)
Flow through depreciation .....	6.0%	17.6%	1.6%
All other, net .....	<u>(9.0%)</u>	<u>1.4%</u>	<u>(1.2%)</u>
	<u>25.4%</u>	<u>31.2%</u>	<u>31.5%</u>

As of December 31, 1998, 1997 and 1996, accumulated deferred income taxes amounted to \$432,299,000, \$408,310,000 and \$334,117,000, respectively, and the unamortized deferred investment tax credits amounted to \$10,609,000, \$12,398,000 and \$13,858,000, respectively. Income taxes paid during the year were \$5,434,000, \$17,765,000 and \$22,525,000 for 1998, 1997 and 1996, respectively.

Notes to Consolidated Financial Statements—(Continued)

The components of the net deferred income tax liability at December 31, are as follows:

	<u>1998</u>	<u>1997</u>	<u>1996</u>
		(\$ in thousands)	
Deferred income tax liabilities:			
Property, plant and equipment basis differences . . . . .	\$334,296	\$338,170	\$285,673
Regulatory assets . . . . .	73,724	76,504	63,447
Other, net . . . . .	<u>47,572</u>	<u>20,101</u>	<u>14,469</u>
	<u>455,592</u>	<u>434,775</u>	<u>363,589</u>
Deferred income tax assets:			
Regulatory liabilities . . . . .	8,431	9,236	10,076
Deferred investment tax credits . . . . .	<u>4,253</u>	<u>4,831</u>	<u>5,538</u>
	<u>12,684</u>	<u>14,067</u>	<u>15,614</u>
Net deferred income tax liability . . . . .	<u>\$442,908</u>	<u>\$420,708</u>	<u>\$347,975</u>

The provision for federal and state income taxes, as well as the taxes charged or credited to shareholders' equity, includes amounts both payable currently and deferred for payment in future periods as indicated below:

	<u>1998</u>	<u>1997</u>	<u>1996</u>
		(\$ in thousands)	
Income taxes charged (credited) to the income statement:			
Current:			
Federal . . . . .	\$ (1,644)	\$13,658	\$19,775
State . . . . .	<u>294</u>	<u>38</u>	<u>(3,256)</u>
Total current . . . . .	<u>(1,350)</u>	<u>13,696</u>	<u>16,519</u>
Deferred:			
Federal . . . . .	23,800	(7,674)	64,895
Investment tax credits . . . . .	(1,627)	(1,740)	(1,865)
State . . . . .	<u>1,514</u>	<u>3,101</u>	<u>5,388</u>
Total deferred . . . . .	<u>23,687</u>	<u>(6,313)</u>	<u>68,418</u>
Subtotal . . . . .	<u>22,337</u>	<u>7,383</u>	<u>84,937</u>
Income tax benefit on dividends on convertible preferred securities:			
Current:			
Federal . . . . .	(3,344)	(3,344)	(3,149)
State . . . . .	<u>(508)</u>	<u>(508)</u>	<u>(479)</u>
Subtotal . . . . .	<u>(3,852)</u>	<u>(3,852)</u>	<u>(3,628)</u>
Income tax benefit on cumulative effect of change in accounting principle:			
Current:			
Federal . . . . .	(478)	—	—
State . . . . .	<u>—</u>	<u>—</u>	<u>—</u>
Subtotal . . . . .	<u>(478)</u>	<u>—</u>	<u>—</u>
Total Income taxes charged to the income statement (a) . . . . .	<u>18,007</u>	<u>3,531</u>	<u>81,309</u>
Income taxes charged (credited) to shareholders' equity:			
Deferred income taxes (benefits) on unrealized gains or losses on securities classified as available-for-sale . . . . .	32,792	6,718	(6,884)
Current benefit arising from stock options exercised . . . . .	<u>(35)</u>	<u>(164)</u>	<u>(345)</u>
Income taxes charged (credited) to shareholders' equity (b) . . . . .	<u>32,757</u>	<u>6,554</u>	<u>(7,229)</u>
Total income taxes: (a) plus (b) . . . . .	<u>\$50,764</u>	<u>\$10,085</u>	<u>\$74,080</u>

**Notes to Consolidated Financial Statements—(Continued)**

The Company's alternative minimum tax credit as of December 31, 1998 is \$74,200,000, which can be carried forward indefinitely to reduce future regular tax liability. The Company's tax net operating loss carry forward as of December 31, 1998 is \$45,400,000, which can be carried forward for 15 years. These benefits are included as debits against accrued income taxes.

**(12) Net Income Per Common Share:**

The reconciliation of the net income per common share calculation for the years ended December 31, 1998, 1997 and 1996 is as follows:

	1998		1997			1996			
	Income	Shares	Per Share	Income	Shares	Per Share	Income	Shares	Per Share
Net income per common share:									
Basic .....	\$57,060	258,879	\$ .22	\$10,100	260,226	\$ .04	\$178,660	261,286	\$ .68
Effect of dilutive options.....	—	742	—	—	598	—	—	802	—
Diluted .....	\$57,060	259,621	\$ .22	\$10,100	260,824	\$ .04	\$178,660	262,088	\$ .68

All share amounts represent weighted average shares outstanding for each respective period. All per share amounts have been adjusted for subsequent stock dividends. The diluted net income per common share calculation excludes the effect of potentially dilutive shares when their exercise price exceeds the average market price over the period. The Company has 4,025,000 shares of potentially dilutive Mandatorily Redeemable Convertible Preferred Securities which are convertible into common stock at a 3.76 to 1 ratio at an exercise price of \$13.30 per share and 6,256,720 potentially dilutive stock options at a range of \$10.31 to \$14.24 per share. These items were adjusted for subsequent stock dividends and were not included in the diluted net income per common share calculation for any of the above periods as their effect was antidilutive.

**(13) Comprehensive Income:**

The Company's other comprehensive income is as follows:

	Year Ended December 31, 1998		
	Before-Tax Amount	Tax Expense/Benefit	Net-of-Tax Amount
Net unrealized gains on securities:			
Net unrealized holding gains arising during period .....	\$56,497	\$21,627	\$34,870
Add: Reclassification adjustment for net losses realized in net income .....	29,167	11,165	18,002
Other comprehensive income .....	<u>\$85,644</u>	<u>\$32,792</u>	<u>\$52,872</u>

**(14) Segment Information:**

The company is a diversified communications and public services company which is segmented into communications, CLEC, gas, electric and water and wastewater services. The communications sector provides both regulated and competitive communications services to residential, business and wholesale customers. The CLEC sector is a facilities based integrated communications provider providing a broad range of communications services throughout the United States through the Company's subsidiary, ELI. The electric sector provides electric transmission and distribution services to primarily residential customers. The gas sector provides natural gas transmission and distribution services to primarily residential customers. The water and wastewater sector provides water distribution, wholesale water transmission, wastewater treatment, public works consulting, and marketing and billing services to residential customers.

Special items charged against revenues represent the revenue portion of the 1997 charges to earnings (see Note 10). Special items charged against operating income represent the 1998 Y2K costs and separation costs, and the 1997 charges to earnings. Sector EBITDA consists of sector operating income plus depreciation. Special items

## Notes to Consolidated Financial Statements—(Continued)

charged against sector EBITDA include Y2K costs and separation costs. Consolidated EBITDA represents the aggregate sector EBITDA plus investment and other income less special items which include 1998 Y2K and separation costs, the 1998 HTCC investment write off, the 1997 non operating gain on sale of subsidiary stock and the 1997 charges to earnings. EBITDA is a measure commonly used to analyze companies on the basis of operating performance. It is not a measure of financial performance under generally accepted accounting principles and should not be considered as an alternative to net income as a measure of performance nor as an alternative to cash flow as a measure of liquidity and may not be compared to similarly titled measures of other companies.

	Year Ended December 31,		
	1998	1997	1996
	(\$ in thousands)		
<b>Communications:</b>			
Revenues excluding special items.....	\$ 867,446	\$ 840,329	\$ 763,459
Inter-sector revenues.....	(32,407)	(23,573)	(11,250)
Revenues as reported .....	835,039	802,589	752,209
Operating income excluding special items.....	164,821	140,143	231,823
Operating income as reported.....	157,567	(2,580)	231,823
Depreciation .....	181,656	175,363	148,022
EBITDA excluding special items.....	346,477	315,506	379,845
EBITDA .....	339,223	172,783	379,845
Capital expenditures, net.....	201,453	263,011	184,041
Total sector assets.....	2,434,183	2,379,936	2,206,092
<b>CLEC:</b>			
Revenues .....	\$ 100,880	\$ 61,084	\$ 35,417
Inter-sector revenues.....	(3,061)	(3,341)	(1,319)
Revenues as reported .....	97,819	57,743	34,098
Operating loss excluding special items.....	(75,647)	(37,436)	(25,286)
Operating loss as reported.....	(75,923)	(48,201)	(25,286)
Depreciation .....	17,002	11,167	5,549
EBITDA excluding special items.....	(58,645)	(26,269)	(19,737)
EBITDA .....	(58,921)	(37,034)	(19,737)
Capital expenditures, net.....	200,000	124,549	41,607
Total sector assets.....	532,309	359,962	206,290
<b>Public Services:</b>			
<i>Gas:</i>			
Revenues .....	\$ 325,423	\$ 252,098	\$ 239,619
Operating income excluding special items.....	43,757	41,907	33,756
Operating income as reported.....	42,225	29,200	33,756
Depreciation .....	24,084	15,587	10,953
EBITDA excluding special items.....	67,841	57,494	44,709
EBITDA .....	66,309	44,787	44,709
Capital expenditures, net .....	45,768	47,880	27,691
Total sector assets.....	554,028	530,696	381,740

Citizens Utilities Company and Subsidiaries

Notes to Consolidated Financial Statements—(Continued)

	Year Ended December 31,		
	1998	1997	1996
	(\$ in thousands)		
<i>Electric:</i>			
Revenues excluding special items.....	\$190,307	\$198,070	\$192,297
Revenues as reported.....	190,307	191,470	192,297
Operating income excluding special items.....	27,746	35,777	24,805
Operating income as reported.....	27,093	13,723	24,805
Depreciation.....	22,733	22,195	18,718
EBITDA excluding special items.....	50,479	57,972	43,523
EBITDA.....	49,826	35,918	43,523
Capital expenditures, net.....	18,895	23,544	24,591
Total sector assets.....	479,210	492,926	482,194
<i>Water and Wastewater:</i>			
Revenues.....	\$ 93,784	\$ 89,719	\$ 88,294
Operating income excluding special items.....	28,140	26,541	30,588
Operating income as reported.....	27,207	23,700	30,588
Depreciation.....	12,369	11,500	10,491
EBITDA excluding special items.....	40,509	38,041	41,079
EBITDA.....	39,576	35,200	41,079
Capital expenditures, net.....	30,793	32,171	21,048
Total sector assets.....	598,397	556,559	511,628

The following table is a reconciliation of certain sector items to the total consolidated amount.

	Year Ended December 31,		
	1998	1997	1996
	(\$ in thousands)		
<b>Revenues</b>			
Total sector revenues excluding special items.....	\$1,577,840	\$1,441,300	\$1,319,086
Inter-sector revenues.....	(35,468)	(26,914)	(12,569)
Charges to earnings.....	—	(20,767)	—
Consolidated reported revenues.....	<u>\$1,542,372</u>	<u>\$1,393,619</u>	<u>\$1,306,517</u>
<b>Operating income</b>			
Total sector operating income excluding special items ....	\$ 188,817	\$ 206,932	\$ 295,686
Y2K costs and separation costs.....	(10,648)	—	—
Charges to earnings.....	—	(191,090)	—
Consolidated reported operating income.....	<u>\$ 178,169</u>	<u>\$ 15,842</u>	<u>\$ 295,686</u>
<b>EBITDA</b>			
Total sector EBITDA excluding special items.....	\$ 446,661	\$ 442,744	\$ 489,419
Investment and other income.....	39,884	42,287	66,455
Minority interest.....	14,032	645	—
HTCC investment write off.....	(31,905)	—	—
Y2K costs and separation costs.....	(10,648)	—	—
Charges to earnings.....	—	(195,576)	—
Non operating gain on sale of subsidiary stock.....	—	78,734	—
Consolidated EBITDA.....	<u>\$ 458,024</u>	<u>\$ 368,834</u>	<u>\$ 555,874</u>

Notes to Consolidated Financial Statements—(Continued)

	Year Ended December 31,		
	1998	1997	1996
	(\$ in thousands)		
<b>Capital expenditures</b>			
Total sector capital expenditures .....	\$ 496,909	\$ 491,155	\$ 298,978
General capital expenditures .....	25,123	33,334	18,785
Consolidated reported capital expenditures .....	<u>\$ 522,032</u>	<u>\$ 524,489</u>	<u>\$ 317,763</u>
<b>Assets</b>			
Total sector assets.....	\$4,598,127	\$4,320,079	\$3,787,944
General assets.....	694,805	552,773	735,204
Consolidated reported assets .....	<u>\$5,292,932</u>	<u>\$4,872,852</u>	<u>\$4,523,148</u>

(15) Quarterly Financial Data (unaudited):

	Revenues	Net Income	Net Income Per Common Share	
			Basic	Dilutive
(\$ in thousands)				
<b>1998</b>				
First quarter .....	\$403,863	\$26,779	\$.10	\$.10
Second quarter .....	366,347	14,462	.06	.06
Third quarter .....	378,279	14,461	.06	.06
Fourth quarter .....	393,883	1,358	.01	.01
(\$ in thousands)				
<b>1997</b>				
First quarter .....	\$375,091	\$ 30,584	\$.12	\$.12
Second quarter .....	308,857	(123,175)	(.47)	(.47)
Third quarter .....	338,803	23,507	.09	.09
Fourth quarter .....	370,868	79,184	.31	.31

First quarter 1998 results include approximately \$2,334,000 after tax cumulative effect of change in accounting principle, net of related minority interest (see Note 1(n)). Fourth quarter 1998 results include an approximate \$19,700,000 after tax write-off of the HTCC investment (see Note 4).

Second quarter 1997 results include approximately \$135,164,000 after tax charges to earnings (see Note 10). Fourth quarter 1997 results include a non-operating \$51,197,000 after tax gain on the sale of subsidiary stock (see Note 11).

The quarterly net income (loss) per common share amounts are rounded to the nearest cent and are adjusted for subsequent stock dividends. Annual earnings per share may vary depending on the effect of such rounding.

## Notes to Consolidated Financial Statements—(Continued)

	Year Ended December 31,		
	1998	1997	1996
	(\$ in thousands)		
<b>Capital expenditures</b>			
Total sector capital expenditures .....	\$ 496,909	\$ 491,155	\$ 298,978
General capital expenditures .....	25,123	33,334	18,785
Consolidated reported capital expenditures .....	<u>\$ 522,032</u>	<u>\$ 524,489</u>	<u>\$ 317,763</u>
<b>Assets</b>			
Total sector assets.....	\$4,598,127	\$4,320,079	\$3,787,944
General assets.....	694,805	552,773	735,204
Consolidated reported assets .....	<u>\$5,292,932</u>	<u>\$4,872,852</u>	<u>\$4,523,148</u>

## (15) Quarterly Financial Data (unaudited):

	Revenues	Net Income	Net Income Per Common Share	
			Basic	Dilutive
	(\$ in thousands)			
<b>1998</b>				
First quarter .....	\$403,863	\$26,779	\$.10	\$.10
Second quarter .....	366,347	14,462	.06	.06
Third quarter .....	378,279	14,461	.06	.06
Fourth quarter .....	393,883	1,358	.01	.01
			Net Income (Loss) Per Common Share	
	Revenues	Net Income (Loss)	Basic	Dilutive
	(\$ in thousands)			
<b>1997</b>				
First quarter .....	\$375,091	\$ 30,584	\$.12	\$.12
Second quarter .....	308,857	(123,175)	(.47)	(.47)
Third quarter .....	338,803	23,507	.09	.09
Fourth quarter .....	370,868	79,184	.31	.31

First quarter 1998 results include approximately \$2,334,000 after tax cumulative effect of change in accounting principle, net of related minority interest (see Note 1(n)). Fourth quarter 1998 results include an approximate \$19,700,000 after tax write-off of the HTCC investment (see Note 4).

Second quarter 1997 results include approximately \$135,164,000 after tax charges to earnings (see Note 10). Fourth quarter 1997 results include a non-operating \$51,197,000 after tax gain on the sale of subsidiary stock (see Note 11).

The quarterly net income (loss) per common share amounts are rounded to the nearest cent and are adjusted for subsequent stock dividends. Annual earnings per share may vary depending on the effect of such rounding.

**Notes to Consolidated Financial Statements—(Continued)**

**(16) Supplemental Cash Flow Information:**

The following is a schedule of net cash provided by operating activities for the years ended December 31, 1998, 1997 and 1996.

	<u>1998</u>	<u>1997</u>	<u>1996</u>
		(\$ in thousands)	
Net income.....	\$ 57,060	\$ 10,100	\$178,660
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation expense .....	257,844	235,812	193,733
Non cash charges to earnings .....	—	153,348	—
Non cash HTCC investment write off .....	31,905	—	—
Cumulative effect of change in accounting principle .....	3,394	—	—
Gain on sale of subsidiary stock .....	—	(78,734)	—
Centennial non cash investment income .....	—	—	(9,043)
Allowance for equity funds used during construction .....	(5,311)	(6,881)	(8,704)
Deferred income tax and investment tax credit .....	23,687	(6,373)	68,418
Change in operating accounts receivable .....	(30,449)	(35,560)	(46,342)
Change in accounts payable and other .....	(102,386)	(36,881)	35,806
Change in accrued taxes and interest .....	18,022	(3,498)	(4,997)
Change in other assets .....	<u>8,602</u>	<u>(901)</u>	<u>(32,350)</u>
Net cash provided by operating activities .....	<u>\$ 262,368</u>	<u>\$230,432</u>	<u>\$375,181</u>

In conjunction with the acquisitions described in Note 3 the Company assumed debt of \$13,800,000, \$8,400,000 and \$13,000,000 in 1998, 1997 and 1996, respectively, at weighted average interest rates of 5.6%, 6.2% and 8.05%, respectively.

**(17) Retirement Plans:**

**Pension Plan**

The Company and its subsidiaries have a noncontributory pension plan covering all employees who have met certain service and age requirements. The benefits are based on years of service and final average pay or career average pay. Contributions are made in amounts sufficient to fund the plan's net periodic pension cost while considering tax deductibility. Plan assets are invested in a diversified portfolio of equity and fixed-income securities.

**Notes to Consolidated Financial Statements—(Continued)**

The following tables set forth the plan's benefit obligations and fair values of plan assets as of December 31, 1998 and 1997.

	<u>1998</u>	<u>1997</u>
	(\$ in thousands)	
<b>Change in benefit obligation</b>		
Benefit obligation at beginning of year .....	\$208,520	\$156,442
Service cost .....	10,747	8,815
Interest cost .....	15,703	12,978
Amendments .....	(1,487)	55
Actuarial loss .....	27,941	22,194
Acquisitions .....	8,344	15,095
Benefits paid .....	<u>(16,854)</u>	<u>(7,059)</u>
Benefit obligation at end of year .....	<u>\$252,914</u>	<u>\$208,520</u>
<b>Change in plan assets</b>		
Fair value of plan assets at beginning of year .....	\$201,834	\$154,151
Actual return on plan assets .....	24,749	25,402
Acquisitions .....	10,875	21,298
Employer contribution .....	11,932	8,042
Benefits paid .....	<u>(16,854)</u>	<u>(7,059)</u>
Fair value of plan assets at end of year .....	<u>\$232,536</u>	<u>\$201,834</u>
<b>Prepaid benefit cost</b>		
Funded status .....	\$ (20,378)	\$ (6,686)
Unrecognized net liability .....	189	233
Unrecognized prior service cost .....	3,682	5,511
Unrecognized net actuarial loss .....	<u>21,807</u>	<u>1,389</u>
Prepaid benefit cost .....	<u>\$ 5,300</u>	<u>\$ 447</u>
<b>Components of net periodic benefit cost</b>		
Service cost .....	\$ 10,747	\$ 8,815
Interest cost on projected benefit obligation .....	15,703	12,978
Return on plan assets .....	(17,241)	(13,764)
Net amortization and deferral .....	<u>400</u>	<u>865</u>
Net periodic benefit cost .....	<u>\$ 9,609</u>	<u>\$ 8,894</u>

Assumptions used in the computation of pension costs/ year end benefit obligations were as follows:

	<u>1998</u>	<u>1997</u>
Discount rate .....	7.5%/7.0%	8.0%/7.5%
Expected long-term rate of return on plan assets .....	8.25%/N/A	8.5%/N/A
Rate of increase in compensation levels .....	4.0%/4.0%	4.0%/4.0%

In November 1998, the Company acquired Rhinelander Telecommunications, Inc., including its pension benefit plans. The acquisition increased the pension benefit obligation by \$3,974,000 and the fair value of plan assets by \$4,884,000 as of December 31, 1998.

**Notes to Consolidated Financial Statements—(Continued)**

In June 1998, the Company acquired TGC, including its non-collectively bargained pension benefit plan. The acquisition increased the pension benefit obligation by \$4,370,000 and the fair value of plan assets by \$5,991,000 as of December 31, 1998.

In October 1997, the Company acquired TGC, including its collectively bargained pension benefit plan. The acquisition increased the pension benefit obligation by \$15,095,000 and the fair value of plan assets by \$21,298,000 as of December 31, 1997.

**Postretirement Benefits Other Than Pensions**

The Company provides certain medical, dental and life insurance benefits for retired employees and their beneficiaries and covered dependents. During 1997, in conjunction with the Company's elimination of its retiree medical and dental plans for all non-union employees who were not eligible to retire, the Company accounted for a negative plan amendment and a curtailment in accordance with SFAS 106, "Employee's Accounting for Postretirement Benefits Other than Pensions."

The following table sets forth the plan's benefit obligations and the postretirement benefit liability recognized on the Company's balance sheets at December 31, 1998 and 1997.

	1998	1997
	(\$ in thousands)	
<b>Change in benefit obligation</b>		
Benefit obligation at beginning of year .....	\$ 49,110	\$ 49,915
Service cost .....	980	1,513
Interest cost .....	3,523	3,878
Plan participants' contributions .....	596	335
Amendments .....	(4,734)	(8,024)
Actuarial loss .....	4,503	2,645
Acquisitions .....	651	259
Benefits paid .....	<u>(2,646)</u>	<u>(1,411)</u>
Benefit obligation at end of year .....	<u>\$ 51,983</u>	<u>\$ 49,110</u>
<b>Change in plan assets</b>		
Fair value of plan assets at beginning of year .....	\$ 6,661	\$ 3,156
Actual return on plan assets .....	677	155
Acquisition .....	—	—
Employer contribution .....	<u>11,372</u>	<u>3,350</u>
Fair value of plan assets at end of year .....	<u>\$ 18,710</u>	<u>\$ 6,661</u>
<b>Accrued benefit cost</b>		
Funded status .....	\$(33,273)	\$(42,449)
Unrecognized transition obligation .....	386	2,494
Unrecognized prior service cost .....	—	—
Accrued benefit cost .....	<u>(7,562)</u>	<u>(12,913)</u>
Net periodic benefit cost .....	<u>\$(40,449)</u>	<u>\$(52,868)</u>
<b>Components of net periodic postretirement benefit costs</b>		
Service cost .....	\$ 980	\$ 1,513
Interest cost on the projected benefit obligation .....	3,523	3,878
Return on plan assets .....	(549)	(268)
Net amortization and deferral .....	(947)	243
Curtailment (gain) charge .....	<u>(2,003)</u>	<u>8,814</u>
Net periodic postretirement benefit cost .....	<u>\$ 1,004</u>	<u>\$ 14,180</u>

For purposes of measuring year end benefit obligations, the Company used the same discount rates as were used for the pension plan and a 7% annual rate of increase in the per-capita cost of covered medical benefits, gradually decreasing to 5% in the year 2040 and remaining at that level thereafter. The effect of a 1% increase in the assumed

**Notes to Consolidated Financial Statements—(Continued)**

medical cost trend rates for each future year on the aggregate of the service and interest cost components of the total postretirement benefit cost would be \$417,000 and the effect on the accumulated postretirement benefit obligation for health benefits would be \$4,854,000. The effect of a 1% decrease in the assumed medical cost trend rates for each future year on the aggregate of the service and interest cost components of the total postretirement benefit cost would be \$(376,000) and the effect on the accumulated postretirement benefit obligation for health benefits would be \$(4,336,000).

**401(k) Savings Plans**

The Company sponsors employee savings plans under section 401(k) of the Internal Revenue Code. The plans cover substantially all full-time employees. Under the plans, the Company provides matching contributions in Company stock based on qualified employee contributions. Matching contributions were \$5,795,000, \$4,883,000 and \$4,248,000 for 1998, 1997 and 1996, respectively.

**(18) Commitments and Contingencies:**

The Company has budgeted capital expenditures in 1999 of approximately \$640,000,000 (includes \$45,000,000 of non-cash capital lease additions) and certain commitments have been entered into in connection therewith.

The Company conducts certain of its operations in leased premises and also leases certain equipment and other assets pursuant to operating leases. Future minimum rental commitments for all long-term noncancelable operating leases are as follows:

<u>Year</u>	<u>Amount</u>
	(\$ in thousands)
1999	\$ 29,393
2000	28,434
2001	26,620
2002	20,137
2003	18,077
thereafter	<u>38,003</u>
Total	<u>\$160,664</u>

Total rental expense included in the Company's results of operations for the years ended December 31, 1998, 1997 and 1996 was \$31,645,000, \$24,207,000 and \$13,146,000, respectively.

In 1995, ELI entered into a \$110 million construction agency agreement and an operating lease agreement in connection with the construction of certain communications networks and fiber cable links. ELI served as agent for the construction of these projects and, upon completion of each project, leased the facilities for a three year term, with one year renewals available through April 30, 2002. At December 31, 1998 and 1997, ELI was leasing assets with an original cost of approximately \$108,541,000 and \$87,426,000, respectively, under this agreement. ELI has the option to purchase the facilities at the end of the lease terms for the amount of the lessor's average investment in the facilities. Payments under the lease depend on current interest rates, and assuming continuation of current interest rates, payments would approximate \$6.1 million annually through April 30, 2002 and, assuming exercise of the purchase option, approximately \$110 million in 2002. In the event ELI chooses not to exercise this option, ELI is obligated to arrange for the sale of the facilities to an unrelated party and is required to pay the lessor any difference between the net sales proceeds and the lessor's investment in the facilities. However, any amount required to be paid to the lessor is subject generally to a maximum of 80% (approximately \$88 million) of the lessor's investment. The Company has guaranteed all obligations of ELI under this operating lease. ELI has agreed to pay the Company a guarantee fee at the rate of 3.25% per annum based on the amount of the lessor's investment in the leased assets.

In June 1998, ELI entered into a private line services agreement with a third party, which allows ELI to utilize the third party's national fiber optic network for a period of nine years. ELI has a total minimum commitment of \$122 million over the term of the agreement, including \$11.6 million in 1999. A portion of the network was operational as of December 31, 1998, with construction on the remainder of the network scheduled for completion in 1999.

**Notes to Consolidated Financial Statements—(Continued)**

The Company is also a party to contracts with several unrelated long distance carriers. The contracts provide fees based on leased traffic subject to minimum monthly fees aggregating \$55,300,000, \$31,200,000 and \$21,200,000 for 1999, 2000, and 2001, respectively.

Under various contracts the Company purchases capacity and associated energy and water from various electric energy, natural gas and water suppliers. Some of these contracts obligate the Company to pay certain capacity costs whether or not energy or water purchases are made. These contracts are intended to complement the other components in the Company's power and water supply to achieve the most economic supply mix reasonably available. The capacity costs for which the Company is obligated are associated with energy and water purchases that approximate 40% of the Company's total annual energy and water costs for 1998. The Company expects this percentage to be no less in future years. At December 31, 1998, the estimated future payments for capacity, energy and water that the Company is obligated to buy under these contracts are as follows:

<u>Year</u>	<u>Amount</u>
	(\$ in thousands)
1999	\$107,095
2000	95,744
2001	93,372
2002	82,218
2003	63,175
thereafter	<u>539,349</u>
Total	<u>\$980,953</u>

The Vermont Joint Owners (VJO), a consortium of 14 Vermont utilities, including the Company, have entered into a purchase power agreement with Hydro-Quebec. The agreement contains "step-up" provisions that state that if any VJO member defaults on its obligation under the contract to purchase power from Hydro-Quebec the other VJO participants will assume responsibility for the defaulting party's share on a pro-rata basis. As of December 31, 1998, the Company's obligation under the agreement is approximately 10% of the total contract. The two largest participants in the VJO represent approximately 46% and 37% of the total contract, respectively. During 1998, these two major participants have each experienced regulatory disallowances that have resulted in credit rating downgrades and stock price declines. Both of these participants are in the process of appealing the regulatory disallowances; however, both companies have stated that an unfavorable ruling could jeopardize their ability to continue as going concerns. If either or both of these companies default on their obligations under the Hydro-Quebec agreement, the remaining members of the VJO, including the Company, may be required to pay for a substantially larger share of the VJO's total power purchase obligation for the remainder of the agreement. Such a result could have a materially adverse effect on the financial results of the Company's Vermont Electric Division and on the Company as a whole.

The Company is involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters, after considering insurance coverages, will not have a material adverse effect on the Company's consolidated financial position, results of operations or liquidity.

## Statement of Responsibility

The management of Citizens Utilities Company is responsible for the preparation of the consolidated financial statements included in this report. The financial statements have been prepared in a manner consistent with generally accepted accounting principles and the accounting policies and procedures prescribed by the appropriate regulatory agencies. Transactions in process at year-end that are required to be included in these financial statements are reflected based on management's informed judgments.

The company maintains internal accounting control systems and related policies and procedures designed to provide reasonable assurance that assets are safeguarded, that transactions are executed as authorized and are properly recorded, and that the accounting records may be relied upon for the preparation of consolidated financial statements and other financial information. There are inherent limitations that should be recognized in considering the assurances provided by any internal control system. Management strives to maintain a balance between the cost of the internal control system and the benefits to be derived.

The company also maintains an internal auditing function which evaluates and formally reports on the adequacy and effectiveness of internal controls, policies and procedures. KPMG LLP, independent certified public accountants, has audited these consolidated financial statements and has expressed its opinion as to their fairness.

The Board of Directors pursues its review and oversight role for these financial statements through an Audit Committee composed of Directors who are not employees of this company. The Audit Committee meets periodically with management and KPMG LLP to review the activities of each in discharging their responsibilities.



Robert J. DeSantis  
*Chief Financial Officer,  
Vice President and Treasurer*

March 5, 1999

## Shareholder Information

### *Common Stock*

Effective August 25, 1997, Citizens Common Stock Series A and Common Stock Series B were combined into a single series common stock trading on the New York Stock Exchange under the symbol CZN.

Citizens has historically declared and issued quarterly stock dividends on its common stock based on the number of whole shares owned on the record date for that dividend. Dividends distributed were paid on both whole and fractional shares to holders of at least one whole share. Under current statutes and regulations, stock dividends are not taxable when received and are treated as capital transactions for federal income tax purposes, when and if sold. Gain or loss is based on the difference between sales price and adjusted basis per share.

Effective with the first quarter of 1999, Citizens Utilities discontinued paying dividends in common stock.

### *Citizens EPPICS*

Citizens declares and issues quarterly distributions on its Equity Providing Preferred Income Convertible Securities (EPPICS). At the option of either Citizens or the holder, distributions are payable in cash or in shares of Citizens common stock. Citizens EPPICS must be purchased through and held by a broker or custodial institution. Please contact your broker, custodial institution or Citizens' Investor Relations department for additional information about this security.

### *Book Entry*

Book entry provides registered shareholders with statements reflecting the number of shares credited to their accounts as a result of direct purchases, stock dividends and stock splits. A shareholder may receive certificates representing his or her direct purchases, stock dividends and stock splits by completing the reverse side of the quarterly statement and mailing it, or a written request, to the company's transfer agent, Illinois Stock Transfer Company (see "Stock Transfer Agent" on the following page).

### *Stock Dividend Sale Plan*

As a result of the discontinuance of common stock dividends, the Stock Dividend Sale Plan is inactive.

### *Direct Stock Purchase and Sale Plan*

Registered shareholders may enroll in Citizens' Direct Stock Purchase and Sale Plan. Street name shareholders may participate in the Plan if their brokers or custodial institutions establish procedures permitting them to do so. The Plan provides shareholders with a convenient method for purchasing additional shares of Citizens common stock by making optional cash payments or by automatic debits from their bank accounts. Under the Plan, the price shareholders pay for Citizens common stock is based on an average market price during the purchase period and includes a commission of two cents per share if the shares are purchased in the open market. There is currently a \$6 transaction fee to purchase stock through the Plan. The Plan also provides shareholders with a way to sell shares of Citizens stock. There is a fee of \$15 and a two cents per share commission for each sales transaction. For information and/or an enrollment form for this Plan, please contact Illinois Stock Transfer Company.

### *Stock Safekeeping Program*

The Safekeeping Program, which is voluntary, allows shareholders to mail their accumulated stock certificates to Citizens' transfer agent, Illinois Stock Transfer Company. Upon receipt, Illinois Stock Transfer credits the shareholder's account with the appropriate number of book entry shares, cancels the actual certificates, and issues a statement reflecting the total number of shares held. Shareholders requiring certificates for sale or pledge may request them in writing (by mail or fax) at any time from the transfer agent. For information about this Program, please contact Illinois Stock Transfer Company.

### Stock Market Information

On February 24, 1992, Citizens commenced trading on the New York Stock Exchange under the symbols CZNA and CZNB for Series A and Series B, respectively. Effective August 25, 1997, Citizens Common Stock Series A and Citizens Common Stock Series B were combined into a single series common stock trading on the New York Stock Exchange under the symbol CZN. Citizens Equity Providing Preferred Income Convertible Securities (EPPICS) is listed on the New York Stock Exchange under the symbol CZNPr.

As of February 26, 1999, the approximate number of registered holders of the company's common stock was 46,592, according to Citizens' transfer agent.

The table below shows the high and low prices per share for the periods shown. These prices were taken from the daily quotations published in *The Wall Street Journal* during the periods indicated. Prices have been adjusted to the nearest 1/16th for subsequent stock dividends.

	1st Quarter		2nd Quarter		3rd Quarter		4th Quarter	
	High	Low	High	Low	High	Low	High	Low
<b>1998</b>								
CZN	\$10 <sup>7</sup> / <sub>8</sub>	\$8 <sup>7</sup> / <sub>8</sub>	\$11 <sup>3</sup> / <sub>16</sub>	\$9 <sup>1</sup> / <sub>2</sub>	\$10	\$6 <sup>7</sup> / <sub>8</sub>	\$9 <sup>1</sup> / <sub>16</sub>	\$7 <sup>1</sup> / <sub>4</sub>
EPPICS	\$49 <sup>13</sup> / <sub>16</sub>	\$47	\$50 <sup>1</sup> / <sub>4</sub>	\$47 <sup>3</sup> / <sub>16</sub>	\$47 <sup>1</sup> / <sub>8</sub>	\$40 <sup>1</sup> / <sub>2</sub>	\$44 <sup>1</sup> / <sub>4</sub>	\$39 <sup>1</sup> / <sub>8</sub>
<b>1997</b>								
CZNA	\$11 <sup>1</sup> / <sub>16</sub>	\$9 <sup>13</sup> / <sub>16</sub>	\$11 <sup>1</sup> / <sub>2</sub>	\$8 <sup>5</sup> / <sub>16</sub>	—	—	—	—
CZNB	\$11 <sup>1</sup> / <sub>16</sub>	\$9 <sup>15</sup> / <sub>16</sub>	\$11 <sup>1</sup> / <sub>2</sub>	\$7 <sup>5</sup> / <sub>8</sub>	\$9	\$7 <sup>9</sup> / <sub>16</sub>	\$10 <sup>1</sup> / <sub>16</sub>	\$8 <sup>13</sup> / <sub>16</sub>
EPPICS	\$52	\$47 <sup>1</sup> / <sub>2</sub>	\$51 <sup>3</sup> / <sub>4</sub>	\$43 <sup>1</sup> / <sub>2</sub>	\$45 <sup>3</sup> / <sub>4</sub>	\$42 <sup>1</sup> / <sub>16</sub>	\$48 <sup>1</sup> / <sub>16</sub>	\$45 <sup>15</sup> / <sub>16</sub>

The December 31, 1998 prices for Citizens common stock were: \$8<sup>1</sup>/<sub>8</sub> high, \$7<sup>15</sup>/<sub>16</sub> low, and for EPPICS: \$42<sup>5</sup>/<sub>8</sub> high, \$42<sup>3</sup>/<sub>8</sub> low.

### Stock Transfer Agent

Questions from registered shareholders concerning stock transfers, the Direct Stock Purchase and Sale Plan, the Stock Safekeeping Program, account consolidations, dividend payments, lost certificates, changes of address, receipt of duplicate material, and any other account-related matters should be directed to Illinois Stock Transfer Company (IST) by telephoning 800.757.5755 or 312.427.2953, or by faxing to 312.427.2879, or by writing to Citizens Utilities, c/o Illinois Stock Transfer Company, 209 West Jackson Boulevard, Suite 903, Chicago, IL 60606-6905.

### Citizens' World Wide Web Site

Anyone with an Internet connection can have online access to company information, including quarterly and annual financial publications, press releases, remarks by Citizens' senior management, historical common stock prices and other information. Citizens' Internet address is: <http://www.czn.net>.

### Shareholder Inquiries

Quarterly financial information is mailed to all shareholders. Questions concerning these materials may be directed to Shareholder Services or Investor Relations at Citizens' Corporate Headquarters by telephoning 800.248.8845. Additional copies of this report, the company's 1998 Form 10-K report filed with the Securities and Exchange Commission, and other written information about the company may be requested by telephoning 800.877.4389, extension 4600; faxing to 203.614.4602; or emailing [Citizens@czn.com](mailto:Citizens@czn.com).

Corporate Headquarters  
Citizens Utilities  
3 High Ridge Park  
Stamford, CT 06905-1390  
Tel. 203.614.5600  
Fax 203.614.4602  
Email [Citizens@czn.com](mailto:Citizens@czn.com)

## Leadership

### *Board of Directors*

Norman I. Borwinik<sup>3,4,5</sup>  
*Director Emeritus of the Board of  
Governors*

*University of New Haven  
New Haven, CT  
Director since 1968*

Aaron I. Fleischman<sup>1,4</sup>  
*Senior Partner, Fleischman and Walsh  
Washington, DC  
Director since 1989*

James C. Goodale<sup>2</sup>  
*Of Counsel, Debevoise & Plimpton  
New York, NY  
Director since 1996*

Stanley Harfenist<sup>1,3,4</sup>  
*President and Chief Executive Officer  
Adesso, Inc.  
Director, Electric Lightwave, Inc.  
Los Angeles, CA  
Director since 1992*

Andrew N. Heine<sup>2</sup>  
*Of Counsel, Gordon Altman Butowsky  
Weitzen Shalov & Wein  
New York, NY  
Director since 1975*

John L. Schroeder<sup>2,5</sup>  
*Director, Morgan Stanley Dean  
Witter Funds  
New York, NY  
Director since 1980*

Robert D. Siff<sup>2</sup>  
*Consultant and former Executive  
Vice President  
Chittenden Bank  
Concord, NH  
Director since 1989*

Robert A. Stanger<sup>1,2,3</sup>  
*Chairman, Robert A. Stanger &  
Co., Inc.  
Director, Electric Lightwave, Inc.  
Shrewsbury, NJ  
Director since 1992*

Charles H. Symington, Jr.<sup>2,3,5</sup>  
*Director, 3i Corporation  
Spring Island, SC  
Director since 1995*

Edwin Tornberg<sup>3,5</sup>  
*President, Edwin Tornberg &  
Co., Inc.  
Potomac, MD  
Director since 1992*

Claire Tow<sup>5</sup>  
*Senior Vice President and Director  
Century Communications Corp.  
New Canaan, CT  
Director since 1993*

Leonard Tow<sup>1</sup>  
*Chairman and Chief Executive  
Officer, Citizens Utilities  
Chairman, Electric Lightwave, Inc.  
Chairman, Century  
Communications Corp.  
Director, Hungarian Telephone &  
Cable Corp.  
Director, United States Telephone  
Association  
Stamford, CT  
Director since 1989*

- 1 Executive Committee
- 2 Audit Committee
- 3 Compensation Committee
- 4 Nominating Committee
- 5 Retirement Committee

### *Officers*

Leonard Tow  
*Chairman and Chief Executive  
Officer*

Daryl A. Ferguson  
*President and Chief Operating Officer*

O. Lee Jobe  
*Vice President, Citizens Utilities  
President, Citizens Communications*

J. Michael Love  
*Vice President, Citizens Utilities  
President, Citizens Public Services*

David B. Sharkey  
*President and Chief Operating Officer  
Electric Lightwave, Inc.*

Kenneth C. Dering  
*Assistant Vice President and Assistant  
Treasurer*

Robert J. DeSantis  
*Chief Financial Officer, Vice President  
and Treasurer*

Laura L. DiPreta  
*Assistant Vice President and Assistant  
Controller*

Nicholas L. Ioli  
*Vice President and Chief Information  
Officer*

Edward O. Kipperman  
*Vice President, Tax*

L. Russell Mitten, II  
*Vice President and General Counsel*

Alan H. Oshiki  
*Assistant Vice President and Assistant  
Treasurer*

Frank E. Plumley  
*Assistant Vice President and Assistant  
Treasurer*

James D. Ranton  
*Vice President, Corporate Human  
Resources*

Livingston E. Ross  
*Vice President and Controller*

Brigid M. Smith  
*Assistant Vice President,  
Corporate Communications*

Donald P. Weinstein  
*Vice President, Planning and  
Development*

Charles J. Weiss  
*Secretary and Assistant Vice President*

**Consolidated Financial Data**

(\$ in thousands, except per-share and other financial data)	Five-Year Compounded Annual Growth	1998	1997	1996	1995	1994
<b>Select Income Statement Data</b>						
Revenues .....	20%	\$1,542,372	\$1,414,386	\$1,306,517	\$1,069,032	\$906,150
Cost of services .....	13%	359,762	333,561	285,749	209,179	203,505
Depreciation .....	36%	257,844	235,812	193,733	158,935	115,175
Other operating expenses .....	29%	735,949	638,081	531,349	446,745	359,346
Operating income .....	3%	188,817	206,932	295,686	254,173	228,124
Special items (1) .....	n/a	(10,648)	(191,090)	—	—	—
Operating income including special items .....	2%	178,169	15,842	295,686	254,173	228,124
Investment and other income .....	—	53,916	42,931	66,455	59,955	52,940
Interest expense .....	25%	112,239	107,584	92,695	87,775	72,744
Special items (2) .....	n/a	(34,239)	72,504	—	—	—
Income taxes .....	-16%	22,337	7,383	84,937	66,817	64,323
Convertible preferred dividends .....	n/a	6,210	6,210	5,849	—	—
Net income .....	-15%	57,060	10,100	178,660	159,536	143,997
Net income excluding special items .....	-7%	85,658	94,087	178,660	159,536	143,997
Net income excluding special items and ELI .....	-1%	120,376	117,912	194,267	170,099	146,054
<b>Cash Flow and Capital Expenditure Data (excludes special items)</b>						
EBITDA (3) .....	13%	\$ 500,577	\$ 485,676	\$ 555,874	\$ 473,063	\$396,239
EBITDA excluding ELI (3) .....	15%	545,190	511,945	575,611	483,787	397,766
Cash flow from operations .....	7%	268,940	260,553	375,181	338,611	262,316
Cash flow from operations excluding ELI ..	9%	305,716	277,742	394,918	349,335	263,843
Capital expenditures .....	27%	522,032	524,489	317,763	240,733	276,876
Capital expenditures excluding ELI .....	16%	322,032	399,940	276,156	213,328	224,067
Free cash flow (4) .....	n/a	(253,092)	(263,936)	57,418	97,878	(14,560)
Free cash flow excluding ELI (4) .....	n/a	(16,316)	(122,198)	118,762	136,007	39,776

(1) For 1998, special items include Y2K and separation costs. For 1997, special items include charges to earnings.

(2) For 1998, special items include the write down of the Company's investment in HTCC and the cumulative effect of a change in accounting principle at ELI. For 1997, special items include the nonoperating gain on sale of subsidiary stock offset by charges to earnings.

(3) Earnings before interest expense, income taxes, depreciation and amortization.

(4) Cash flow from operations less capital expenditures.

Citizens Utilities Company and Subsidiaries

**Consolidated Financial Data**

(\$ in thousands, except per-share and other financial data)	Five-Year Compounded Annual Growth	1998	1997	1996	1995	1994
<b>Select Balance Sheet Data</b>						
Cash and investments.....	-3%	\$ 446,683	\$ 433,662	\$ 563,382	\$ 347,012	\$ 448,053
Total assets.....	15%	5,292,932	4,872,852	4,523,148	3,918,187	3,576,566
Net plant.....	19%	4,048,623	3,667,793	3,138,052	2,908,030	2,569,655
Long-term debt.....	28%	1,900,246	1,706,532	1,509,697	1,187,000	994,189
Equity (5).....	15%	1,994,021	1,880,461	1,879,433	1,559,913	1,156,896
Shares of common stock outstanding.....	7%	259,149	250,994	239,148	227,587	193,472
Weighted average shares outstanding (6).....	2%	258,879	260,226	261,286	250,484	236,619
<b>Per-Share Data (6)</b>						
Basic and diluted net income per share of common stock as reported.....	-16%	\$ .22	\$ .04	\$ .68	\$ .64	\$ .61
Basic net income per share of common stock excluding special items.....	-9%	\$ .33	\$ .36	\$ .68	\$ .64	\$ .61
Basic net income per share of common stock excluding special items and ELI.....	-3%	\$ .47	\$ .45	\$ .74	\$ .68	\$ .62
Operating cash flow per share ...	4%	\$1.01	\$ .89	\$1.44	\$1.35	\$1.11
Operating cash flow per share excluding special items.....	5%	\$1.04	\$1.00	\$1.44	\$1.35	\$1.11
Operating cash flow per share excluding special items and ELI	7%	\$1.18	\$1.07	\$1.51	\$1.39	\$1.12
Book value per share.....	11%	\$6.93	\$6.45	\$6.42	\$6.23	\$4.89
<b>Other Financial Data</b>						
Long-term debt to long-term debt and equity.....	n/a	49%	48%	45%	43%	46%
Long-term debt to long-term debt and equity excluding ELI.....	n/a	44%	47%	45%	43%	46%
Interest coverage (7).....	n/a	4.1x	3.4x	6.0x	5.4x	5.4x
Interest coverage excluding special items (7).....	n/a	4.5x	4.5x	6.0x	5.4x	5.4x
Interest coverage excluding special items and ELI (7).....	n/a	4.9x	4.8x	6.2x	5.5x	5.5x
Common equity market capitalization (in billions).....	n/a	\$ 2.1	\$ 2.4	\$ 2.6	\$ 2.9	\$ 2.5
Equity market capitalization (in billions) (8).....	n/a	\$ 2.2	\$ 2.6	\$ 2.8	\$ 2.9	\$ 2.5
Market capitalization (in billions) (9).....	n/a	\$ 4.1	\$ 4.4	\$ 4.4	\$ 4.2	\$ 3.5
ELI public enterprise value (in billions) (10).....	n/a	\$ .7	\$ .8	n/a	n/a	n/a

(5) Includes convertible preferred securities.

(6) Adjusted for subsequent stock dividends and stock splits and used in the calculation of all per share data.

(7) EBITDA divided by interest expense.

(8) Includes market value of convertible preferred securities.

(9) Equity market capitalization plus market value of long-term debt.

(10) Includes common equity market capitalization plus net debt.

**Sector Financial and Operating Data**

(\$ in thousands, except operating data)	Five-Year Compounded Annual Growth	1998	1997	1996	1995	1994
		<b>Citizens Communications</b>				
<b>Select Income Statement Data</b>						
<b>Revenues</b>						
Network access services.....	30%	\$ 432,018	\$ 403,990	\$ 391,151	\$ 334,952	\$ 265,532
Local network services.....	45%	262,239	250,521	232,904	197,092	139,896
Long distance services.....	n/a	96,584	104,914	59,072	14,217	—
Directory services.....	35%	31,691	31,982	30,248	24,866	17,843
Other.....	27%	44,914	48,922	50,084	29,486	25,452
Eliminations (1).....	n/a	(32,407)	(23,573)	(11,250)	(1,436)	—
<b>Total revenues</b> .....	<b>36%</b>	<b>835,039</b>	<b>816,756</b>	<b>752,209</b>	<b>599,177</b>	<b>448,723</b>
Cost of services (network expenses).....	n/a	89,514	96,303	61,432	10,372	—
Depreciation.....	52%	181,656	175,363	148,022	114,218	79,853
Other operating expenses.....	45%	434,516	431,861	323,501	285,428	216,817
Eliminations (1).....	n/a	(35,468)	(26,914)	(12,569)	(2,151)	—
<b>Operating income</b> .....	<b>14%</b>	<b>164,821</b>	<b>140,143</b>	<b>231,823</b>	<b>191,310</b>	<b>152,053</b>
Special items (2).....	n/a	(7,254)	(142,723)	—	—	—
Operating income/(loss) including special items.....	13%	157,567	(2,580)	231,823	191,310	152,053
Operating margin.....	n/a	20%	17%	31%	32%	34%
<b>Cash Flow and Capital Expenditure Data</b>						
Operating cash flow (3).....	26%	\$ 346,477	\$ 315,506	\$ 379,845	\$ 305,528	\$ 231,906
Capital expenditures.....	37%	201,453	263,011	184,041	113,657	120,416
Free cash flow (4).....	17%	145,024	52,495	195,804	191,871	111,490
EBITDA margin (5).....	n/a	41%	39%	50%	51%	52%
<b>Select Balance Sheet Data</b>						
Total assets.....	23%	\$2,434,183	\$2,379,936	\$2,206,092	\$1,973,198	\$1,691,647
Net plant.....	22%	2,122,794	2,024,220	1,843,298	1,702,989	1,456,439
<b>Operating Data</b>						
Access lines.....	23%	951,513	895,880	834,180	776,764	705,517
Long distance customers - in territory....	n/a	230,871	236,000	179,133	47,049	—
- out of territory.....	n/a	8,101	22,000	40,003	6,785	—
- total.....	n/a	238,972	258,000	219,136	53,834	—
Revenue per access line.....	11%	\$ 878	\$ 912	\$ 902	\$ 771	\$ 636
In-territory billed access minutes of use (in millions).....	n/a	4,526	4,496	4,251	3,168	—
Citizens' long distance minutes of use (in millions) - in territory.....	n/a	483	435	212	74	—
- out of territory.....	n/a	221	414	174	11	—
- total.....	n/a	704	849	386	85	—
Citizens' long distance in territory minutes of use market share.....	n/a	19%	20%	16%	2%	—
Citizens' long distance in territory customer market share.....	n/a	24%	27%	21%	6%	—

(1) The Company began providing long distance services in 1995. Eliminations represent network access revenues received by the Company's local exchange operations from its long-distance and competitive local exchange operations.

(2) For 1998, special items include Y2K and separation costs. For 1997, special items include the charge to earnings.

(3) Operating income excluding special items plus depreciation. This is the equivalent of sector EBITDA.

(4) Operating cash flow less capital expenditures.

(5) Operating cash flow divided by total revenues.

Citizens Utilities Company and Subsidiaries

**Sector Financial and Operating Data**

(\$ in thousands, except operating data)	Five-Year Compounded Annual Growth	1998	1997	1996	1995	1994
<b>Electric Lightwave, Inc.(1)</b>						
<b>Select Income Statement Data</b>						
<i>Revenues</i>						
Network services .....	n/a	\$ 36,589	\$ 33,522	\$ 19,947	\$ 14,357	\$ 7,041
Local telephone services .....	n/a	38,169	10,565	2,533	676	—
Long distance services .....	n/a	12,309	8,140	7,232	1,586	—
Data services .....	n/a	13,813	8,857	5,705	1,666	1,111
Eliminations (1) .....	n/a	(3,061)	(3,341)	(1,319)	(715)	—
<b>Total revenues</b> .....	n/a	97,819	57,743	34,098	17,570	8,152
Cost of services (network expenses) .....	n/a	50,957	29,546	15,782	7,405	6,155
<b>Gross margin</b> .....	n/a	46,862	28,197	18,316	10,165	1,997
Depreciation .....	n/a	17,002	11,167	5,549	6,390	1,806
Other operating expenses .....	n/a	105,507	54,466	38,053	20,889	3,524
<b>Operating loss</b> .....	n/a	(75,647)	(37,436)	(25,286)	(17,114)	(3,333)
Special items (2) .....	n/a	(276)	(10,765)	—	—	—
<b>Operating loss including special items</b> ...	n/a	(75,923)	(48,201)	(25,286)	(17,114)	(3,333)
<b>Cash Flow and Capital Expenditure Data</b>						
Operating cash flow (3) .....	n/a	\$ (58,645)	\$ (26,269)	\$ (19,737)	\$ (10,724)	\$ (1,527)
Capital expenditures .....	n/a	200,000	124,549	41,607	27,405	52,809
<b>Free cash flow (4)</b> .....	n/a	(258,645)	(150,818)	(61,344)	(38,129)	(54,336)
<b>Select Balance Sheet Data</b>						
Total assets .....	n/a	\$ 532,309	\$ 359,962	\$ 206,290	\$ 124,079	\$ 114,246
Gross plant - owned .....	n/a	528,582	328,664	156,738	119,975	106,174
- leased .....	n/a	108,541	87,426	62,485	43,446	11,334
- total .....	n/a	637,123	416,090	219,223	163,421	117,508
<b>Operating Data</b>						
Route miles .....	n/a	3,091	2,494	1,428	780	601
Fiber miles .....	n/a	181,368	140,812	97,665	52,013	37,504
Customers .....	n/a	1,644	1,165	763	402	221
Buildings connected .....	n/a	766	610	438	282	191
Employees .....	n/a	1,090	573	402	225	127
<b>Revenue per employee</b> .....	n/a	\$ 89,742	\$ 100,773	\$ 84,821	\$ 78,089	\$ 64,189

(1) The Company's Competitive Local Exchange Carrier (CLEC) subsidiary, Electric Lightwave, Inc. (ELI). Eliminations reflect intercompany activity between the Company's CLEC and communications operations.

(2) For 1998, special items include Y2K and separation costs. For 1997, special items include the charge to earnings.

(3) Operating loss excluding special items plus depreciation. This is the equivalent of sector EBITDA.

(4) Operating cash flow less capital expenditures.

**Sector Financial and Operating Data**

(\$ in thousands, except operating data)	Five-Year Compounded Annual Growth	1998	1997	1996	1995	1994
<b>Citizens Public Services</b>						
<b>Select Income Statement Data</b>						
<i>Revenues</i>						
Residential distribution .....	6%	\$ 307,440	\$ 298,866	\$ 285,626	\$ 245,983	\$ 247,002
Commercial distribution .....	13%	181,669	135,671	119,260	105,045	104,047
Industrial distribution .....	4%	87,924	74,856	85,238	75,182	71,333
Total distribution .....	7%	577,033	509,393	490,124	426,210	422,382
Transportation/transmission .....	-13%	2,435	2,622	5,519	4,255	3,846
Other .....	2%	30,046	27,872	24,567	21,820	23,047
<b>Total revenues</b> .....	<b>7%</b>	<b>609,514</b>	<b>539,887</b>	<b>520,210</b>	<b>452,285</b>	<b>449,275</b>
Cost of services (1) .....	6%	254,759	234,626	221,104	193,553	197,350
<b>Gross margin</b> .....	<b>8%</b>	<b>354,755</b>	<b>305,261</b>	<b>299,106</b>	<b>258,732</b>	<b>251,925</b>
Depreciation .....	13%	59,186	49,282	40,162	38,327	33,516
Other operating expenses .....	8%	195,926	151,754	169,795	140,428	139,005
<b>Operating income</b> .....	<b>6%</b>	<b>99,643</b>	<b>104,225</b>	<b>89,149</b>	<b>79,977</b>	<b>79,404</b>
Special items (2) .....	n/a	(3,118)	(37,602)	—	—	—
<b>Operating income including special items</b>	<b>5%</b>	<b>96,525</b>	<b>66,623</b>	<b>89,149</b>	<b>79,977</b>	<b>79,404</b>
<b>Cash Flow and Capital Expenditure Data</b>						
Operating cash flow (3) .....	8%	\$ 158,829	\$ 153,507	\$ 129,311	\$ 118,304	\$ 112,920
Capital expenditures .....	3%	95,456	103,595	73,330	89,466	82,902
<b>Free cash flow (4)</b> .....	<b>20%</b>	<b>63,373</b>	<b>49,912</b>	<b>55,981</b>	<b>28,838</b>	<b>30,018</b>
<b>Select Balance Sheet Data</b>						
Total assets .....	8%	\$1,631,635	\$1,580,181	\$1,375,562	\$1,337,780	\$1,220,749
Net plant .....	9%	1,344,643	1,269,271	1,096,928	1,052,841	971,006
<b>Operating Data</b>						
Customers .....	4%	867,300	845,600	765,452	749,633	730,653
Employees .....	5%	1,787	1,719	1,519	1,489	1,531
Customers per employee .....	-1%	485	492	504	503	477
<b>Gross margin (net revenue) per employee</b>	<b>3%</b>	<b>\$ 198,520</b>	<b>\$ 177,581</b>	<b>\$ 196,910</b>	<b>\$ 173,762</b>	<b>\$ 164,549</b>

(1) Natural gas, electric energy and fuel oil purchased.

(2) For 1998, special items include Y2K and separation costs. For 1997, special items include the charge to earnings.

(3) Operating income excluding special items plus depreciation. This is the equivalent of sector EBITDA.

(4) Operating cash flow less capital expenditures.

Citizens Utilities Company and Subsidiaries

**Financial and Operating Data by Service**

(\$ in thousands, except operating data)	Five-Year Compounded Annual Growth	1998	1997	1996	1995	1994
<b>Citizens Public Services</b>						
<b>Gas</b>						
<b>Select Income Statement Data</b>						
<i>Revenues</i>						
Residential distribution .....	5%	\$150,386	\$145,016	\$134,888	\$110,146	\$117,266
Commercial distribution .....	21%	109,259	64,004	49,633	40,614	43,497
Industrial distribution .....	6%	47,497	30,366	40,230	35,244	35,342
Total distribution .....	9%	307,142	239,386	224,751	186,004	196,105
Transportation .....	-13%	2,435	2,622	5,519	4,255	3,846
Other .....	8%	15,846	10,090	9,349	7,643	8,989
<b>Total revenues</b> .....	<b>9%</b>	<b>325,423</b>	<b>252,098</b>	<b>239,619</b>	<b>197,902</b>	<b>208,940</b>
Cost of services (natural gas purchased) ..	7%	166,829	139,900	127,913	108,385	116,419
<b>Gross margin</b> .....	<b>11%</b>	<b>158,594</b>	<b>112,198</b>	<b>111,706</b>	<b>89,517</b>	<b>92,521</b>
Depreciation .....	18%	24,084	15,587	10,953	12,155	10,827
Other operating expenses .....	11%	90,753	54,704	66,997	51,488	51,489
<b>Operating income</b> .....	<b>9%</b>	<b>43,757</b>	<b>41,907</b>	<b>33,756</b>	<b>25,874</b>	<b>30,205</b>
Special items (1) .....	n/a	(1,532)	(12,707)	—	—	—
<b>Operating income including special items</b>	<b>8%</b>	<b>42,225</b>	<b>29,200</b>	<b>33,756</b>	<b>25,874</b>	<b>30,205</b>
<b>Cash Flow and Capital Expenditure Data</b>						
Operating cash flow (2) .....	11%	\$ 67,841	\$ 57,494	\$ 44,709	\$ 38,029	\$ 41,032
Capital expenditures .....	14%	45,768	47,880	27,691	28,659	26,247
<b>Free cash flow (3)</b> .....	<b>7%</b>	<b>22,073</b>	<b>9,614</b>	<b>17,018</b>	<b>9,370</b>	<b>14,785</b>
<b>Select Balance Sheet Data</b>						
Total assets .....	14%	\$554,028	\$530,696	\$381,740	\$344,036	\$306,979
Net plant .....	15%	444,126	423,533	281,220	261,326	240,667
<b>Operating Data</b>						
Customers .....	6%	457,200	446,100	371,244	363,293	356,343
Employees .....	5%	958	923	799	776	795
Customers per employee .....	—	477	483	465	468	448
Gross margin (net revenue) per employee	5%	\$165,547	\$121,558	\$139,807	\$115,357	\$116,379
Billion Cubic Feet of gas throughput						
(BCF) .....	8%	108.8	80.3	73.9	83.0	71.3

(1) For 1998, special items include Y2K and separation costs. For 1997, special items include the charge to earnings.

(2) Operating income excluding special items plus depreciation. This is the equivalent of sector EBITDA.

(3) Operating cash flow less capital expenditures.

**Financial and Operating Data by Service**

(\$ in thousands, except operating data)	Five-Year Compounded					
	Annual Growth	1998	1997	1996	1995	1994
<b>Citizens Public Services</b>						
<b>Electric</b>						
<b>Select Income Statement Data</b>						
<b>Revenues</b>						
Residential distribution .....	5%	\$ 80,887	\$ 83,108	\$ 79,893	\$ 72,460	\$ 71,322
Commercial distribution .....	5%	57,617	57,455	55,826	52,152	49,597
Industrial distribution .....	3%	39,393	43,529	44,165	39,362	35,376
Total distribution .....	4%	177,897	184,092	179,884	163,974	156,295
Other .....	-2%	12,410	13,978	12,413	11,377	11,645
<b>Total revenues</b> .....	<b>4%</b>	<b>190,307</b>	<b>198,070</b>	<b>192,297</b>	<b>175,351</b>	<b>167,940</b>
Cost of services (electric energy and fuel oil purchased) .....	3%	87,930	94,726	93,191	85,168	80,931
<b>Gross margin</b> .....	<b>5%</b>	<b>102,377</b>	<b>103,344</b>	<b>99,106</b>	<b>90,183</b>	<b>87,009</b>
Depreciation .....	12%	22,733	22,195	18,718	17,035	15,251
Other operating expenses .....	7%	51,898	45,372	55,583	43,088	40,537
<b>Operating income</b> .....	<b>-2%</b>	<b>27,746</b>	<b>35,777</b>	<b>24,805</b>	<b>30,060</b>	<b>31,221</b>
Special items (1) .....	n/a	(653)	(22,054)	—	—	—
<b>Operating income including special items</b> ..	<b>-2%</b>	<b>27,093</b>	<b>13,723</b>	<b>24,805</b>	<b>30,060</b>	<b>31,221</b>
<b>Cash Flow and Capital Expenditure Data</b>						
Operating cash flow (2) .....	3%	\$ 50,479	\$ 57,972	\$ 43,523	\$ 47,095	\$ 46,472
Capital expenditures .....	-12%	18,895	23,544	24,591	32,849	34,379
<b>Free cash flow (3)</b> .....	<b>30%</b>	<b>31,584</b>	<b>34,428</b>	<b>18,932</b>	<b>14,246</b>	<b>12,093</b>
<b>Select Balance Sheet Data</b>						
Total assets .....	1%	\$ 479,210	\$ 492,926	\$ 482,194	\$ 487,893	\$ 458,457
Net plant .....	3%	386,299	388,162	393,475	389,036	363,237
<b>Operating Data</b>						
Customers .....	3%	115,400	111,800	109,802	107,274	104,269
Employees .....	-3%	300	303	345	342	377
Customers per employee .....	6%	385	369	318	314	277
Gross margin (net revenue) per employee ..	8%	\$ 341,257	\$ 341,069	\$ 287,264	\$ 263,693	\$ 230,793
Megawatt hours sold .....	4%	1,745,419	1,655,121	1,691,384	1,594,814	1,562,115
Megawatt hours generated .....	3%	367,285	353,390	352,261	360,276	327,036
Megawatt hours purchased .....	4%	1,533,163	1,533,584	1,395,073	1,331,495	1,333,092

(1) For 1998, special items include Y2K and separation costs. For 1997, special items include the charge to earnings.

(2) Operating income excluding special items plus depreciation. This is the equivalent of sector EBITDA.

(3) Operating cash flow less capital expenditures.

**Financial and Operating Data by Service**

(\$ in thousands, except operating data)	Five-Year Compounded					
	Annual Growth	1998	1997	1996	1995	1994
<b>Citizens Public Services</b>						
<b>Water/Wastewater</b>						
<b>Select Income Statement Data</b>						
<i>Revenues</i>						
Residential distribution .....	8%	\$ 76,167	\$ 70,742	\$ 70,845	\$ 63,377	\$ 58,414
Commercial distribution .....	9%	14,793	14,212	13,801	12,279	10,953
Industrial distribution .....	19%	1,034	961	843	576	615
Other .....	-5%	1,790	3,804	2,805	2,800	2,413
<b>Total revenues</b> .....	<b>7%</b>	<b>93,784</b>	<b>89,719</b>	<b>88,294</b>	<b>79,032</b>	<b>72,395</b>
Depreciation .....	8%	12,369	11,500	10,491	9,137	7,438
Other operating expenses .....	5%	53,275	51,678	47,215	45,852	46,979
<b>Operating income</b> .....	<b>13%</b>	<b>28,140</b>	<b>26,541</b>	<b>30,588</b>	<b>24,043</b>	<b>17,978</b>
Special items (1) .....	n/a	(933)	(2,841)	—	—	—
<b>Operating income including special items</b>	<b>12%</b>	<b>27,207</b>	<b>23,700</b>	<b>30,588</b>	<b>24,043</b>	<b>17,978</b>
<b>Cash Flow and Capital Expenditure Data</b>						
Operating cash flow (2) .....	11%	\$ 40,509	\$ 38,041	\$ 41,079	\$ 33,180	\$ 25,416
Capital expenditures .....	6%	30,793	32,171	21,048	27,958	22,276
<b>Free cash flow (3)</b> .....	<b>53%</b>	<b>9,716</b>	<b>5,870</b>	<b>20,031</b>	<b>5,222</b>	<b>3,140</b>
<b>Select Balance Sheet Data</b>						
Total assets .....	8%	\$598,397	\$556,559	\$511,628	\$505,851	\$455,312
Net plant .....	11%	514,218	457,576	422,233	402,479	367,102
<b>Operating Data</b>						
Customers .....	3%	294,700	287,700	284,406	279,066	270,041
Employees .....	2%	352	364	375	371	359
Customers per employee .....	1%	837	790	758	752	752
Revenue per employee .....	6%	\$266,432	\$246,481	\$235,451	\$213,024	\$201,657
Billions of gallons of water delivered ....	—	29.6	31.4	32.5	31.2	29.9
Billions of gallons of wastewater treated .	3%	5.1	5.0	5.6	5.6	4.7

(1) For 1998, special items include Y2K and separation costs. For 1997, special items include the charge to earnings.

(2) Operating income excluding special items plus depreciation. This is the equivalent of sector EBITDA.

(3) Operating cash flow less capital expenditures.

**CITIZENS UTILITIES COMPANY**

**FORM 10-Q**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)**

**OF THE SECURITIES EXCHANGE ACT OF 1934**

**FOR THE QUARTERLY PERIOD ENDED JUNE 30, 1999**

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 1999

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 001-11001

CITIZENS UTILITIES COMPANY

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of  
incorporation or organization)

06-0619596

(I.R.S. Employer Identification No.)

3 High Ridge Park  
P.O. Box 3801

Stamford, Connecticut

(Address of principal executive offices)

06905

(Zip Code)

Registrant's telephone number, including area code (203) 614-5600

NONE

(Former name, former address and former fiscal year, if changed since last report.)

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 twelve 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 ninety days.

Yes X No   

The number of shares outstanding of the registrant's class of common stock as of July 31, 1999 was 260,553,664.

**PART I. FINANCIAL INFORMATION**

**CITIZENS UTILITIES COMPANY AND SUBSIDIARIES  
CONSOLIDATED BALANCE SHEETS**

(In thousands)

	<u>June 30, 1999</u>	<u>December 31, 1998</u>
<b><u>ASSETS</u></b>		
Current assets:		
Cash	\$ 27,596	\$ 31,922
Accounts receivable, net	294,038	318,378
Other	56,649	63,741
Total current assets	<u>378,283</u>	<u>414,041</u>
Property, plant and equipment	6,262,406	5,947,353
Less accumulated depreciation	2,044,416	1,898,730
Net property, plant and equipment	<u>4,217,990</u>	<u>4,048,623</u>
Investments	435,762	414,761
Regulatory assets	204,875	204,703
Deferred debits and other assets	233,579	210,804
Total assets	<u>\$ 5,470,489</u>	<u>\$ 5,292,932</u>
<b><u>LIABILITIES AND EQUITY</u></b>		
Current liabilities:		
Long-term debt due within one year	\$ 23,878	\$ 8,930
Short-term debt	-	110,000
Accounts payable and current liabilities	430,604	388,801
Total current liabilities	<u>454,482</u>	<u>507,731</u>
Deferred income taxes	423,259	442,908
Customer advances for construction	201,305	211,941
Deferred credits and other liabilities	98,317	96,827
Regulatory liabilities	19,224	19,120
Long-term debt	2,106,514	1,900,246
Total liabilities	<u>3,303,101</u>	<u>3,178,773</u>
Company Obligated Mandatorily Redeemable Convertible Preferred Securities *	201,250	201,250
Contributions in aid of construction	95,713	90,353
Minority interest in subsidiary	19,658	29,785
Shareholders' equity:		
Common stock issued, \$.25 par value	65,075	64,787
Additional paid-in capital	1,563,929	1,554,188
Retained earnings	179,482	117,104
Accumulated other comprehensive income	42,281	56,692
Total shareholders' equity	<u>1,850,767</u>	<u>1,792,771</u>
Total liabilities and shareholders' equity	<u>\$ 5,470,489</u>	<u>\$ 5,292,932</u>

\* Represents securities of a subsidiary trust, the sole assets of which are securities of a subsidiary partnership, substantially all the assets of which are convertible debentures of the Company.

The accompanying Notes are an integral part of these Financial Statements.

F I. FINANCIAL INFORMATION (Continued)

**CITIZENS UTILITIES COMPANY AND SUBSIDIARIES**  
**CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME**  
**FOR THE SIX MONTHS ENDED JUNE 30, 1999 AND 1998**  
(In thousands, except per-share amounts)

	<u>1999</u>	<u>1998</u>
Revenues	\$ 852,361	\$ 770,210
Operating expenses:		
Cost of services	197,299	188,727
Depreciation	152,125	128,362
Other operating expenses	435,193	355,338
Total operating expenses	<u>784,617</u>	<u>672,427</u>
Income from operations	67,744	97,783
Other income, net	81,536	18,321
Minority interest	11,686	5,136
Interest expense	<u>60,366</u>	<u>55,395</u>
Income before income taxes, dividends on convertible preferred securities and cumulative effect of change in accounting principle	100,600	65,845
Income taxes	<u>35,118</u>	<u>19,166</u>
Income before dividends on convertible preferred securities and cumulative effect of change in accounting principle	65,482	46,679
Dividends on convertible preferred securities, net of income tax benefit	<u>3,104</u>	<u>3,104</u>
Income before cumulative effect of change in accounting principle	62,378	43,575
Cumulative effect of change in accounting principle, net of income tax benefit and related minority interest	<u>-</u>	<u>2,334</u>
Net income	62,378	41,241
Other comprehensive income (loss), net of tax and reclassification adjustment	<u>(14,411)</u>	<u>23,284</u>
Total comprehensive income	<u>\$ 47,967</u>	<u>\$ 64,525</u>
Net income per common share before cumulative effect of change in accounting principle:		
Basic	\$ .24	\$ .17 *
Diluted	\$ .24	\$ .17 *
Net income per common share:		
Basic	\$ .24	\$ .16 *
Diluted	\$ .24	\$ .16 *
Compounded dividend rate declared on common stock	<u>-</u>	<u>1.51%</u>

\* Adjusted for subsequent stock dividends.

The accompanying Notes are an integral part of these Financial Statements.

Part I. FINANCIAL INFORMATION (Continued)

CITIZENS UTILITIES COMPANY AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Summary of Significant Accounting Policies:

(a) Basis of Presentation:

The unaudited consolidated financial statements include the accounts of Citizens Utilities Company and its subsidiaries (the Company) and have been prepared in conformity with generally accepted accounting principles. These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company's 1998 Annual Report on Form 10-K. These unaudited consolidated financial statements include all adjustments, which consist of normal recurring accruals necessary to present fairly the results for the interim periods shown. Certain information and footnote disclosures have been condensed pursuant to Securities and Exchange Commission rules and regulations. The results of the interim periods are not necessarily indicative of the results for the full year. Certain reclassifications of balances previously reported have been made to conform to current presentation.

(b) Regulatory Assets and Liabilities:

The Company's regulated operations are subject to the provisions of Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation." SFAS 71 requires regulated entities to record regulatory assets and liabilities as a result of actions of regulators.

(c) Net Income Per Common Share:

Basic net income per common share is computed using the weighted average number of common shares outstanding during the period being reported on. Diluted net income per common share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock at the beginning of the period being reported on. In 1998, both Basic and Diluted net income per common share calculations are presented with adjustments for subsequent stock dividends.

(d) Change in Accounting Principle:

In April 1998, the Accounting Standards Executive Committee of the AICPA released Statement of Position (SOP) 98-5, "Reporting on the Costs of Start-Up Activities." SOP 98-5 requires that the unamortized portion of deferred start-up costs be written off and reported as a change in accounting principle. Future costs of start-up activities should then be expensed as incurred. Certain third party direct costs incurred by Electric Lightwave, Inc. (ELI) in connection with negotiating and securing initial rights-of-way and developing network design for new market clusters or locations had been capitalized by ELI in previous years and were being amortized over five years. The Company adopted SOP 98-5 effective January 1, 1998. The net book value of these deferred amounts was \$3,394,000 which has been reported as a cumulative effect of a change in accounting principle in the statements of income and comprehensive income for the first quarter 1998, net of income tax benefit of \$577,000 and related minority interest of \$483,000.

(2) Separation:

On May 18, 1998, the Company announced its plans to separate its communications businesses and public services businesses into two stand-alone publicly traded companies. The Company had planned to transfer to NewTelecom all of its telecommunications businesses, including its approximate 82% ownership interest in ELI. This separation was subject to federal and state regulatory approvals and was expected to be carried out through a distribution of the stock of NewTelecom to the Company's shareholders. The public services businesses were to continue to operate as Citizens Utilities Company and provide natural gas transmission and distribution, electric transmission and distribution, water distribution and wastewater treatment services. This separation was being made in recognition of the different investment features, performance criteria, capital structures, dividend policies, customers' requirements and regulatory designs of each business, and would have allowed each business to pursue its own strategy and to compete more effectively in its respective markets. Through May 1999, the Company had been pursuing its separation plans, however, other opportunities have since become available to acquire telecommunications properties which have resulted in the Company's desire to no longer pursue separation plans.

On May 27, 1999 the Company announced that it has entered into definitive agreements to purchase from GTE Corporation 187,000 telephone access lines (as of year-end 1998) in Arizona, California and Minnesota for approximately \$664,000,000 in cash. The Company expects that the acquisition, which is subject to various state and federal regulatory approvals, is expected to be completed in 2000.

ART I. FINANCIAL INFORMATION (Continued)

CITIZENS UTILITIES COMPANY AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(4) Sale of Investments:

In January 1999, Centennial Cellular Corp. (Centennial) was merged with CCW Acquisition Corp., a company organized at the direction of Welsh, Carson, Anderson & Stowe. The Company was a holder of 1,982,294 shares of Centennial Class B Common Stock. In addition, as a holder of 102,187 shares of Mandatorily Redeemable Convertible Preferred Stock of Centennial, the Company was required to convert the preferred stock into approximately 2,972,000 shares of Class B Common Stock. The Company received approximately \$205,600,000 in cash for all of its Common Stock interests and approximately \$17,500,000 related to accrued dividends on the preferred stock. The Company recorded a pre-tax gain of approximately \$69,500,000 on this transaction in January 1999 which is included in other income, net.

In March 1999, Adelphia Communication Corporation (Adelphia) and Century Communications Corp. (Century) announced the signing of a definitive agreement for the merger of Century with Adelphia. The Company currently owns 1,807,095 shares of Century Class A Common Stock. Pursuant to the merger agreement, each Century Class A Common Share will be exchanged for cash of \$9.16 and .6122 of a share of Adelphia Class A Common Stock (for a total market value of \$46.20 per Century Class A Common Share based on Adelphia's July 29, 1999 closing price of \$60.50.) This transaction is expected to close during the fourth quarter of 1999.

A subsidiary of the Company, in a joint venture with a subsidiary of Century, acquired and operates four cable television systems in southern California serving over 90,000 basic subscribers. The Company accounts for the joint venture following the equity method of accounting. The Company has entered into an agreement to sell its interest in the joint venture to Adelphia. Pursuant to this agreement, the Company will receive approximately \$27,700,000 in cash and 1,852,302 shares of Adelphia Class A Common Stock (for a total market value of \$139,764,000 based on Adelphia's July 29, 1999 closing price of \$60.50.) This transaction is expected to close concurrent with the merger of Adelphia and Century.

(5) Segment Information:

The Company is a diversified communications and public services company which is segmented into communications, CLEC, gas, electric and water and wastewater services. The communications sector provides both regulated and competitive communications services to residential, business and wholesale customers. The CLEC sector is a facilities based integrated communications provider providing a broad range of communications services throughout the United States through the Company's subsidiary, ELI. The gas sector provides gas transmission and distribution services to primarily residential customers. The electric sector provides electric transmission and distribution services to primarily residential customers. The water and wastewater sector provides water distribution, wholesale water transmission, wastewater treatment and public works consulting services to primarily residential customers and also provides marketing and billing services to others.

Special items charged against operating income and sector EBITDA during 1999 and 1998 include Y2K and separation costs (see Note 2). Sector EBITDA consists of sector operating income plus depreciation. EBITDA is a measure commonly used to analyze companies on the basis of operating performance. It is not a measure of financial performance under generally accepted accounting principles and should not be considered as an alternative to net income as a measure of performance nor as an alternative to cash flow as a measure of liquidity and may not be compared to similarly titled measures of other companies.

PART I. FINANCIAL INFORMATION (Continued)

CITIZENS UTILITIES COMPANY AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The following table is a reconciliation of certain sector items to the total consolidated amount.

	For the three months ended June 30,		For the six months ended June 30,	
	(\$ in thousands)		(\$ in thousands)	
	1999	1998	1999	1998
<u>Operating income</u>				
Total sector operating income excluding special items	\$ 41,647	\$ 41,905	\$ 84,389	\$ 98,583
Y2K and separation costs	(10,226)	(400)	(16,645)	(800)
Consolidated reported operating income	<u>\$ 31,421</u>	<u>\$ 41,505</u>	<u>\$ 67,744</u>	<u>\$ 97,783</u>
<u>EBITDA</u>				
Total sector EBITDA excluding special items	\$ 118,131	\$ 106,670	\$ 236,514	\$ 226,945
Investment and other income	6,344	7,683	12,037	18,321
Gain on sale of Centennial	-	-	69,499	-
Minority interest	5,693	3,053	11,686	5,136
Y2K and separation costs	(10,226)	(400)	(16,645)	(800)
Consolidated EBITDA	<u>\$ 119,942</u>	<u>\$ 117,006</u>	<u>\$ 313,091</u>	<u>\$ 249,602</u>

PART I. FINANCIAL INFORMATION (Continued)

CITIZENS UTILITIES COMPANY AND SUBSIDIARIES

(a) Liquidity and Capital Resources

The Company considers its operating cash flows and its ability to raise debt and equity capital as the principal indicators of its liquidity. For the six months ended June 30, 1999, the Company used cash flow from operations and proceeds from net financings and parties desiring utility services to fund capital expenditures. Funds requisitioned from the Industrial Development Revenue Bond construction fund trust accounts were used to partially fund the construction of utility plant.

The Company has committed revolving lines of credit with commercial banks under which it may borrow up to \$575,000,000. There were no amounts outstanding under these lines at June 30, 1999. ELI has committed revolving lines of credit with commercial banks under which it may borrow up to \$400,000,000. The Company has guaranteed all of ELI's obligations under these revolving lines of credit. As of June 30, 1999, \$130,000,000 was outstanding under ELI's revolving lines of credit. In April 1999, ELI completed an offering of \$325 million of five-year senior unsecured notes. The notes have an interest rate of 6.05% and mature on May 15, 2004. The Company has guaranteed the payment of principal, any premium and interest on the notes when due.

In January 1999, Centennial Cellular Corp. (Centennial) was merged with CCW Acquisition Corp., a company organized at the direction of Welsh, Carson, Anderson & Stowe. The Company was a holder of 1,982,294 shares of Centennial Class B Common Stock. In addition, as a holder of 102,187 shares of Mandatorily Redeemable Convertible Preferred Stock of Centennial, the Company was required to convert the preferred stock into approximately 2,972,000 shares of Class B Common Stock. The Company received approximately \$205,600,000 in cash for all of its Common Stock interests and approximately \$17,500,000 related to accrued dividends on the preferred stock. The Company recorded a pre-tax gain of approximately \$69,500,000 on this transaction in January 1999 which is included in other income, net.

In March 1999, Adelphia Communication Corporation (Adelphia) and Century Communications Corp. (Century) announced the signing of a definitive agreement for the merger of Century with Adelphia. The Company currently owns 1,807,095 shares of Century Class A Common Stock. Pursuant to the merger agreement, each Century Class A Common Share will be exchanged for cash of \$9.16 and .6122 of a share of Adelphia Class A Common Stock (for a total market value of \$46.20 per Century Class A Common Share based on Adelphia's July 29, 1999 closing price of \$60.50.) This transaction is expected to close during the fourth quarter of 1999.

A subsidiary of the Company, in a joint venture with a subsidiary of Century, acquired and operates four cable television systems in southern California serving over 90,000 basic subscribers. The Company accounts for the joint venture following the equity method of accounting. The Company has entered into an agreement to sell its interest in the joint venture to Adelphia. Pursuant to this agreement, the Company will receive approximately \$27,700,000 in cash and 1,852,302 shares of Adelphia Class A Common Stock (for a total market value of \$139,764,000 based on Adelphia's July 29, 1999 closing price of \$60.50.) This transaction is expected to close concurrent with the merger of Adelphia and Century.

In May 1999, in connection with HTCC's debt restructuring, the Company cancelled HTCC's \$8,400,000 note obligation and the seven-year consulting services agreement in exchange for the issuance by HTCC to the Company of 1,300,000 shares of HTCC common stock and 30,000 shares of HTCC's 5% convertible preferred stock. Each share of HTCC convertible preferred stock has a liquidation value of \$70 and is convertible at the option of the Company into 10 shares of HTCC common stock. To the extent the 1,300,000 HTCC common shares and the 300,000 HTCC common shares underlying the HTCC convertible preferred stock do not achieve an average market closing price of at least \$7 per share during a certain period prior to March 31, 2000, HTCC has agreed to issue additional HTCC convertible preferred shares with a value equal to any such shortfall.

## Part I. FINANCIAL INFORMATION (Continued)

### CITIZENS UTILITIES COMPANY AND SUBSIDIARIES

Certain public services state regulatory commissions, where the Company operates, have issued orders allowing the deferral of Y2K costs for consideration in future rate proceedings. In accordance with these orders the Company deferred \$2,388,000 in 1999.

The systems of vendors and suppliers play a major role in the conduct of the business of the Company. As a result, as part of its Y2K program, the Company has been contacting software suppliers to determine major areas of exposure to Y2K issues. The Company has also been contacting its major suppliers and service providers to ascertain their ability to comply. In addition, the Company contracted with a consulting firm to review the Y2K programs of selected third party vendors. Thus far, most of these parties have stated that they intend to be Y2K compliant by the year 2000. However, there can be no guarantee that the systems of suppliers or service providers on which the Company's systems rely will be compliant, or that failure to be compliant by another company, or a conversion that is incompatible with the Company's systems, would not have a material adverse effect on the Company.

The Company's communications businesses rely, directly and/or indirectly, on a large number of traffic carriers to carry communications traffic through a series of interconnected chains of communications. Therefore, despite its efforts, the Company cannot ensure that each entity involved in the delivery of communications services will be Y2K compliant. In an effort to address third party compliance issues, the Company's communications sector has initiated testing activities with one of its major suppliers.

The electric power-supply systems of North America are connected into four major interconnections called grids. Operational component failures of any entity connected to any of the grids could cause failures in that grid. The Company continues to assess these risks as the millennium approaches to evaluate the likelihood of failures and develop approaches for mitigating the risk of failures. In addition, the Company participates in trade associations such as the Electric Power Research Institute (EPRI) and the American Gas Association (AGA), which furthers the industry's efforts toward Y2K readiness. The Company uses these organizations' Y2K programs' vast resources to accelerate its Y2K program for embedded systems. They also provide a forum for working within the industry peer group whereby joint conclusions may be reached on other key aspects of Y2K readiness. EPRI's Y2K program participants represent more than 70% of the electric power generation capacity in the U.S. AGA represents 181 natural gas utilities that deliver gas to homes and businesses in all fifty states.

The Company has completed approximately 90% of its Y2K remediation efforts on mission critical systems and products so as to ensure continued delivery of core business activities to our customers. Testing, remediation and monitoring will continue through the remainder of 1999 to verify that there are no outstanding problems that either were not captured during the initial Y2K efforts or arose after June 30, 1999. Also, review, modifications and testing of the contingency plans will take place throughout the remainder of 1999 and into the year 2000.

The Contingency Plans for the Company was completed to meet the June 30, 1999 milestone. The plans are dedicated to ensuring that established and expected levels of customer service are maintained without interruption, while core business functionality is preserved during the millennium transition. Additionally, the plans utilize existing operating policies and procedures, disaster recovery plans, and enterprise prioritization of all systems and applications by examining potential exposures while documenting clear mitigation strategies. Contingency planning, risk mitigation, and testing activities will continue through the year rollover by all Company organizations.

The extent and magnitude of the Y2K problem is difficult to predict or quantify. The above information is based on the Company's best estimates which were made using numerous assumptions, including the availability and future costs of certain technological and other resources, third party modification actions and other factors. Given the complexity of the issue and the possibility of unidentified risks, actual results may vary materially from those discussed above. Specific factors that might cause such differences include, among others, the availability and cost of the personnel trained in this area, the ability to locate and correct all affected computer codes, the timing and success of remedial efforts of third party suppliers and similar uncertainties.

PART I. FINANCIAL INFORMATION (Continued)

CITIZENS UTILITIES COMPANY AND SUBSIDIARIES

	For the three months ended June 30, (\$ in thousands)			For the six months ended June 30, (\$ in thousands)		
	1999	1998	% Increase/ (Decrease)	1999	1998	% Increase/ (Decrease)
<b>CLEC revenues</b>						
Network services	\$ 12,983	\$ 8,371	55%	\$ 23,407	\$ 17,478	34%
Local telephone services	18,600	7,769	139%	32,908	13,793	139%
Long distance services	9,245	1,899	387%	17,775	3,721	378%
Data services	5,267	3,404	55%	10,221	6,508	57%
Eliminations	(770)	(740)	N/A	(1,468)	(1,615)	N/A
	<u>\$ 45,325</u>	<u>\$ 20,703</u>	119%	<u>\$ 82,843</u>	<u>\$ 39,885</u>	108%

Network services revenues for the three and six months ended June 30, 1999 increased \$4.6 million, or 55%, and \$5.9 million, or 34%, respectively, as compared with the prior year periods primarily due to sales of additional circuits to new and existing customers, partially offset by the expiration of a short-term contract with a significant customer in the first quarter of 1999.

Local telephone services revenues for the three and six months ended June 30, 1999 increased \$10.8 million, or 139%, and \$19.1 million, or 139%, respectively, as compared with the prior year periods primarily due to an increase in reciprocal compensation revenues that are earned under various interconnection agreements. In addition, increased sales of the integrated service digital network (ISDN) product to Internet Service Providers and an increase in local dial tone services contributed to the increase.

Long distance services revenues for the three and six months ended June 30, 1999 increased \$7.3 million, or 387%, and \$14.1 million, or 378%, respectively, as compared with the prior year periods primarily due to increases in prepaid services resulting from new large volume customers.

Data services revenues for the three and six months ended June 30, 1999 increased \$1.9 million, or 55%, and \$3.7 million, or 57%, respectively, as compared with the prior year periods primarily due to increased sales from Internet and frame relay services.

Eliminations reflect intercompany activity between the Company's CLEC and communications sectors.

T I. FINANCIAL INFORMATION (Continued)

**CITIZENS UTILITIES COMPANY AND SUBSIDIARIES**

	For the three months ended June 30,			For the six months ended June 30,		
	(\$ in thousands)			(\$ in thousands)		
	1999	1998	% Increase/ (Decrease)	1999	1998	% Increase/ (Decrease)
<b>Electric revenues</b>						
Residential	\$ 18,359	\$ 17,732	4%	\$ 38,685	\$ 38,511	0%
Commercial	14,405	13,269	9%	27,998	26,433	6%
Industrial	10,794	9,633	12%	20,053	19,710	2%
Municipal	1,966	2,036	(3%)	3,944	3,931	0%
Total Distribution	45,524	42,670	7%	90,680	88,585	2%
Transportation	48	917	(95%)	953	1,488	(36%)
Other	1,590	212	650%	1,603	1,000	60%
	<u>\$ 47,162</u>	<u>\$ 43,799</u>	8%	<u>\$ 93,236</u>	<u>\$ 91,073</u>	2%

Electric revenues for the three and six months ended June 30, 1999 increased \$3.4 million, or 8%, and \$2.2 million, or 2%, respectively, as compared with the prior year periods primarily due to higher purchased electric energy and fuel oil costs passed on to customers and increased consumption.

	For the three months ended June 30,			For the six months ended June 30,		
	(\$ in thousands)			(\$ in thousands)		
	1999	1998	% Increase/ (Decrease)	1999	1998	% Increase/ (Decrease)
<b>Water and Wastewater revenues</b>						
Residential distribution	\$ 18,226	\$ 17,784	2%	\$ 35,820	\$ 34,197	5%
Commercial distribution	4,657	3,347	39%	7,799	6,255	25%
Industrial distribution	291	237	23%	523	447	17%
Other	1,610	1,051	53%	3,376	1,986	70%
	<u>\$ 24,784</u>	<u>\$ 22,419</u>	11%	<u>\$ 47,518</u>	<u>\$ 42,885</u>	11%

Water and wastewater revenues for the three and six months ended June 30, 1999 increased \$2.4 million, or 11%, and \$4.6 million, or 11%, respectively, as compared with the prior year periods primarily due to customer growth, increased consumption and rate increases in Ohio in January 1999 and California in November 1998.

ART I. FINANCIAL INFORMATION (Continued)

CITIZENS UTILITIES COMPANY AND SUBSIDIARIES

	For the three months ended June 30,			For the six months ended June 30,		
	(\$ in thousands)			(\$ in thousands)		
	1999	1998	% Increase/ (Decrease)	1999	1998	% Increase/ (Decrease)
<b>Other Operating Expenses</b>						
Operating and maintenance	\$ 172,456	\$ 146,930	17%	\$ 345,065	\$ 286,863	20%
Taxes other than income	27,239	21,899	24%	55,935	48,873	14%
Sales and marketing	17,630	10,553	67%	34,193	19,602	74%
	<u>\$ 217,325</u>	<u>\$ 179,382</u>	21%	<u>\$ 435,193</u>	<u>\$ 355,338</u>	22%

Operating and maintenance expenses for the three and six months ended June 30, 1999 increased \$25.5 million, or 17%, and \$58.2 million, or 20%, respectively, as compared with the prior year periods primarily due to increased CLEC operating expenses as a result of the CLEC national data expansion, increased Y2K and separation expenses and the acquisition of RTI.

Taxes other than income for the three and six months ended June 30, 1999 increased \$5.3 million, or 24%, and \$7.1 million or 14%, respectively, as compared with the prior year periods primarily due to an increase in payroll and property taxes.

Sales and marketing expenses for the three and six months ended June 30, 1999 increased \$7.1 million, or 67%, and \$14.6 million, or 74%, respectively, as compared with the prior year periods primarily due to increased personnel and product advertising to support the delivery of services in existing and new markets including the CLEC national data expansion.

**OTHER INCOME, NET/MINORITY INTEREST/INTEREST EXPENSE/INCOME TAXES**

	For the three months ended June 30,			For the six months ended June 30,		
	(\$ in thousands)			(\$ in thousands)		
	1999	1998	% Increase/ (Decrease)	1999	1998	% Increase/ (Decrease)
<b>Other Income, Net</b>						
Investment income	\$ 6,191	\$ 7,851	(21%)	\$ 80,802	\$ 16,622	386%
Other	153	(168)	191%	734	1,699	(57%)
	<u>\$ 6,344</u>	<u>\$ 7,683</u>	(17%)	<u>\$ 81,536</u>	<u>\$ 18,321</u>	345%

Investment income for the three months ended June 30, 1999 decreased \$1.7 million or 21% as compared with the prior year period primarily due to lower average investment balances. Investment income for the six months ended June 30, 1999 increased \$64.2 million, or 386%, as compared with the prior year period primarily due to the \$69.5 million gain on the sale of the Company's investment in Centennial in January 1999 partially offset by lower investment income earned due to lower average investment balances.

Other income for the three months ended June 30, 1999 increased \$.3 million, or 191%, as compared with the prior year period primarily due to a supplemental sales program for the supply of natural gas, offset by a decrease in the equity component of Allowance for Funds Used during Construction. Other income for the six months ended June 30, 1999 decreased \$1 million or 57% as compared with the prior year period primarily due to a decrease in the equity component of Allowance for Funds Used during Construction.

## ART I. FINANCIAL INFORMATION (Continued)

## CITIZENS UTILITIES COMPANY AND SUBSIDIARIES

NET INCOME AND NET INCOME PER COMMON SHARE

	For the three months ended June 30, (\$ in thousands)			For the six months ended June 30, (\$ in thousands)		
	1999	1998	% Increase/ (Decrease)	1999	1998	% Increase/ (Decrease)
Net income	\$ 7,753	\$ 14,462	(46%)	\$ 62,378	\$ 41,241	51%
Net income per common share:						
Basic	\$ .03	\$ .06	(50%)	\$ .24	\$ .16	50%
Diluted	\$ .03	\$ .06	(50%)	\$ .24	\$ .16	50%

Net income and net income per share for the three months ended June 30, 1999 decreased \$6.7 million, or 46%, and .03¢, or 50%, respectively, as compared with the prior year period primarily due to increased losses from the Company's CLEC subsidiary and Y2K and separation costs. Net income and net income per share for the six months ended June 30, 1999 increased \$21.1 million, or 51%, and .08¢, or 50%, respectively, as compared with the prior year period primarily due to the first quarter \$69.5 million gain on the sale of the Company's investment in Centennial.

**PART II. OTHER INFORMATION**  
**CITIZENS UTILITIES COMPANY AND SUBSIDIARIES**

**Item 1. Legal Proceedings**

In November 1995, the Company's Vermont electric division was permitted an 8.5% rate increase. Subsequently, the Vermont Public Service Board (VPSB) called into question the level of rates awarded the Company in connection with its formal review of allegations made by the Department of Public Service (the DPS), the consumer advocate in Vermont and a former Citizens employee. The major issues in this proceeding involved classification of certain costs to property, plant and equipment accounts and the Company's Demand Side Management program. In addition, the DPS believed that the Company should have sought and received regulatory approvals prior to construction of certain facilities in prior years. On June 16, 1997, the VPSB ordered the Company to reduce its rates for Vermont electric service by 14.65% retroactive to November 1, 1995 and to refund to customers, with interest, all amounts collected since that time in excess of the rates authorized by the VPSB. In addition, the VPSB assessed statutory penalties totaling \$60,000 and placed the Company on regulatory probation for a period of at least five years. During this probationary period, the Company could lose its franchise to operate in Vermont if it violates the terms of probation prescribed by the VPSB. The VPSB prescribed final terms of probation in its final order issued September 15, 1998. In October 1998, the Company filed an appeal in the Vermont Supreme Court challenging certain of the penalties imposed by the VPSB.

In August 1997, a lawsuit was filed in the United States District Court for the District of Connecticut (Leventhal vs. Tow, et al.) against the Company and five of its officers, one of whom is also a director, on behalf of all persons who purchased or otherwise acquired Series A and Series B shares of Common Stock of the Company between September 5, 1996 and July 11, 1997, inclusive. On February 9, 1998, the plaintiffs filed an amended complaint. The complaint alleged that Citizens and the individual defendants, during such period, violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 based upon certain public statements made by the Company, which are alleged to be materially false or misleading, or are alleged to have failed to disclose information necessary to make the statements made not false or misleading. The plaintiffs sought to recover unspecified compensatory damages. The Company and the individual defendants believed the allegations are unfounded and filed a motion to dismiss on March 27, 1998. On March 30, 1999 the Court dismissed the action. On April 29, 1999 the plaintiffs filed a notice of appeal with the Court of Appeals for the Second Circuit.

In March 1998, a lawsuit was filed in the United States District Court for the District of Connecticut (Ganino vs. Citizens Utilities Company, et al.), against the Company and three of its officers, one of whom is also a director, on behalf of all purchasers of the Company's Common Stock between May 6, 1996 and August 7, 1997, inclusive. The complaint alleges that the Company and the individual defendants, during such period, violated Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 by making materially false and misleading public statements concerning the Company's relationship with a purported affiliate, Hungarian Telephone and Cable Corp. (HTCC), and by failing to disclose material information necessary to render prior statements not misleading. The plaintiff seeks to recover unspecified compensatory damages. The Company and the individual defendants believe that the allegations are unfounded and filed a motion to dismiss. The plaintiff requested leave to file an amended complaint and an amended complaint was served on the Company on July 24, 1998. The Company's motion to dismiss the amended complaint was filed on October 13, 1998. The Court dismissed the action with prejudice on June 28, 1999.

In November 1998, a class action lawsuit was filed in state District Court for Jefferson Parish, Louisiana, against the Company and three of its subsidiaries: LGS Natural Gas Company, LGS Intrastate, Inc. and Louisiana General Service Company. The lawsuit alleges that the Company and the other named defendants passed through in rates charged to Louisiana customers certain costs that plaintiffs contend were unlawful. The lawsuit seeks compensatory damages in the amount of the alleged overcharges and punitive damages equal to three times the amount of any compensatory damages, as allowed under Louisiana law. In addition, the Louisiana Public Service Commission has opened an investigation into the allegations raised in the lawsuit. The Company and its subsidiaries believe that the allegations made in the lawsuit are unfounded and the Company will vigorously defend its interests in both the lawsuit and the related Commission investigation.

In addition, the Company is party to various other legal proceedings arising in the normal course of business. The outcome of individual matters is not predictable. However, management believes that the ultimate resolution of all such matters, including those discussed above, after considering insurance coverages, will not have a material adverse effect on the Company's financial position, results of operations, or its cash flows.

ART II. OTHER INFORMATION (Continued)  
CITIZENS UTILITIES COMPANY AND SUBSIDIARIES

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CITIZENS UTILITIES COMPANY  
(Registrant)

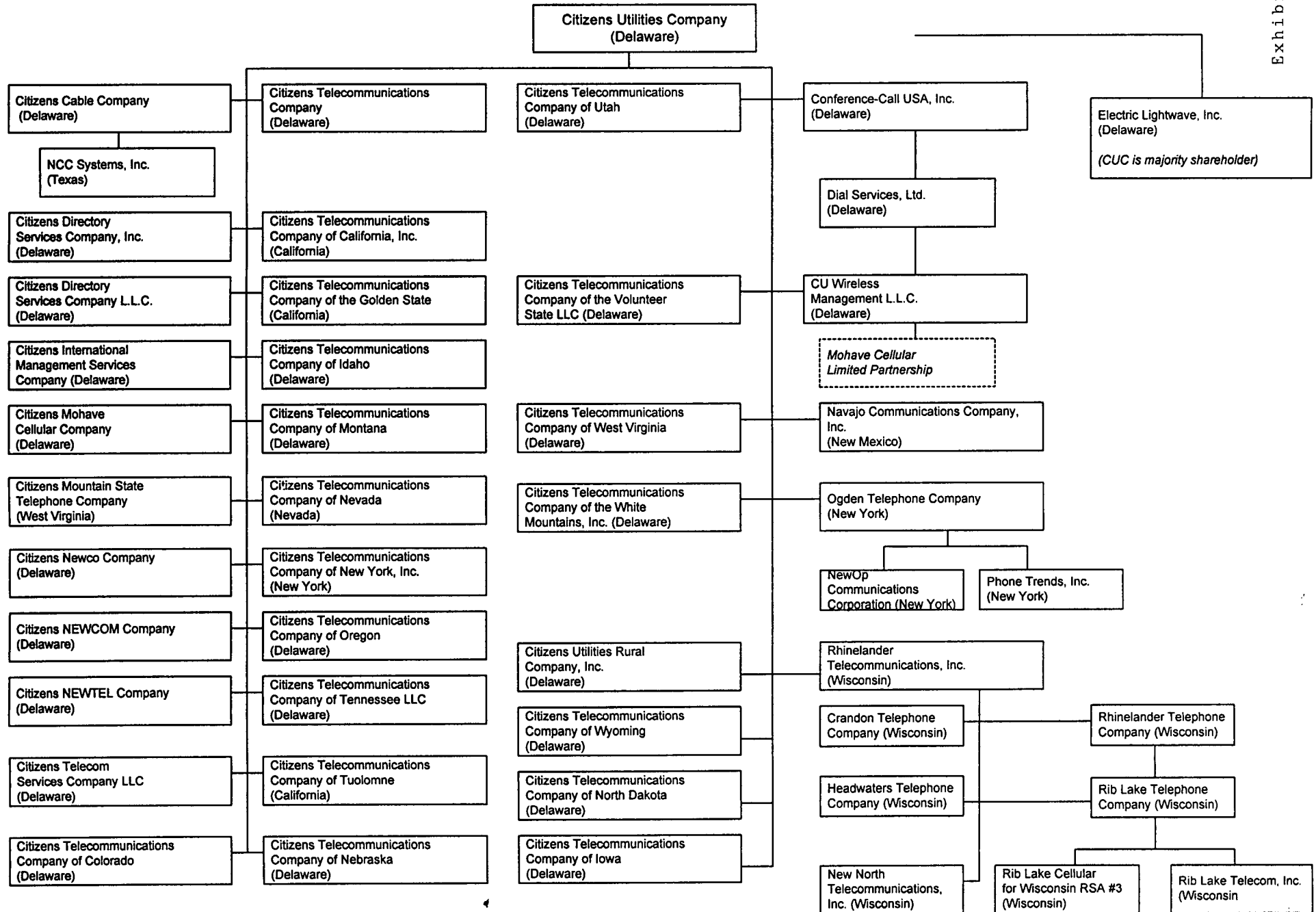
By: /s/ Robert J. DeSantis  
Robert J. DeSantis  
Chief Financial Officer,  
Vice President and Treasurer

By: /s/ Livingston E. Ross  
Livingston E. Ross  
Vice President and Controller

Date: August 5, 1999

**Citizens Utilities Company  
Communications Subsidiaries and States of Incorporation  
As of September 9, 1999**

Exhibit 7



PU-2304-00-270

**SENDER: COMPLETE THIS SECTION**

- Complete items 1, 2, and 3. Also complete item 4 if Restricted Delivery is desired.
- Print your name and address on the reverse so that we can return the card to you.
- Attach this card to the back of the mailpiece, or on the front if space permits.

1. Article Addressed to:

Charles A Lippman  
 Master Edelman Summit Brand  
 3300 Norwood Ctr 908 7th St  
 Minneapolis Mn 5542-4140

2. Article Number (Copy from service label)

7000 0520 0022 8654 0421

PS Form 3811, July 1999

Domestic Return Receipt

102595-99-M-1789

**COMPLETE THIS SECTION ON DELIVERY**

A. Received by (Please Print Clearly) B. Date of Delivery  
 2/12/01

C. Signature  
 X D. Ives  Agent  
 Addressee

D. Is delivery address different from item 1?  Yes  
 If YES, enter delivery address below:  No

3. Service Type  
 Certified Mail  Express Mail  
 Registered  Return Receipt for Merchandise  
 Insured Mail  C.O.D.

4. Restricted Delivery? (Extra Fee)  Yes

PU-2304-00-270

**SENDER: COMPLETE THIS SECTION**

- Complete items 1, 2, and 3. Also complete item 4 if Restricted Delivery is desired.
- Print your name and address on the reverse so that we can return the card to you.
- Attach this card to the back of the mailpiece, or on the front if space permits.

1. Article Addressed to:

Charles Lippman  
 Master Edelman Summit Brand  
 3300 Norwood Ctr 908 7th St  
 Minneapolis Mn 5542-4140

2. Article Number (Copy from service label)

7099 3220 0002 8476 9033

PS Form 3811, July 1999

Domestic Return Receipt

102595-99-M-1789

**COMPLETE THIS SECTION ON DELIVERY**

A. Received by (Please Print Clearly) B. Date of Delivery  
 8/25/10

C. Signature  
 X Harry Law  Agent  
 Addressee

D. Is delivery address different from item 1?  Yes  
 If YES, enter delivery address below:  No

3. Service Type  
 Certified Mail  Express Mail  
 Registered  Return Receipt for Merchandise  
 Insured Mail  C.O.D.

4. Restricted Delivery? (Extra Fee)  Yes