ORIGINAL

NEW APPLICATION

0000027422

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October 6, 2005

VIA OVERNIGHT DELIVERY

Docket Control Center
Arizona Corporation Commission
1200 W. Washington Street
Phoenix, Arizona 85007
(602) 542-2237

Re: Inter-Tel NetSolutions, Inc.

T-02585A-05-0710

Dear Sir/Madam:

Enclosed please find for filing an original and thirteen (13) copies of Inter-Tel NetSolutions, Inc.'s Application and Petition for Certificate of Public Convenience and Necessity to Provide Competitive Resold Local Exchange Telecommunications Services.

I have also enclosed an extra copy of this letter to be date stamped and returned to me in the enclosed, self-addressed, postage prepaid envelope.

If you have any questions or if I may provide you with any additional information, please do not hesitate to contact me. Thank you for your attention to this matter.

Respectfully submitted,

Lance J.M. Steinhart
Attorney for Inter-Tel NetSolutions, Inc.

RECEIVED
2005 OCT -7 P 12: 56
AZ CORP COMMISSION
DOCUMENT CONTROL

Enclosures
cc: Jon Brinton
Christa Fallin w/o encl.
Michael W. Patten, Esq. (2-Day Delivery)

07/14/03

ARIZONA CORPORATION COMMISSION

Application and Petition for Certificate of Convenience and Necessity to Provide Intrastate Telecommunications Services

Mail original plus 13 copies of completed application to:

Docket Control Center
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007-2927

For Docket Control Only:
(Please Stamp Here)

Please indicate if you have current applications pending in Arizona as an Interexchange reseller, AOS provider, or as the provider of other telecommunication services.

Type of Service: ______________________

Docket No.: __________ Date: __________ Date Docketed: ______________

Type of Service: ______________________

Docket No.: __________ Date: __________ Date Docketed: ______________

A. COMPANY AND TELECOMMUNICATION SERVICE INFORMATION

(A-1) Please indicate the type of telecommunications services that you want to provide in Arizona and answer the appropriate numbered items:

☐ Resold Long Distance Telecommunications Services (Answer Sections A, B).

☒ Resold Local Exchange Telecommunications Services (Answer Sections A, B, C).

☐ Facilities-Based Long Distance Telecommunications Services (Answer Sections A, B, D).

☐ Facilities-Based Local Exchange Telecommunications Services (Answer Sections A, B, C, D, E)

☐ Alternative Operator Services Telecommunications Services (Answer Sections A, B)

(A-2) The name, address, telephone number (including area code), facsimile number (including area code), e-mail address, and World Wide Web address (if one is available for consumer access) of the Applicant:

Inter-Tel NetSolutions, Inc.
4310 East Cotton Center Blvd., Suite A-100
Phoenix, Arizona 85040
Telephone: (602) 253-6004
Fax: (602) 532-4128
E-Mail Address: jon_brinton@inter-tel.com
Web Address: www.inter-tel.com

(A-3) The d/b/a ("Doing Business As") name if the Applicant is doing business under a name different from that listed in Item (A-2):

(A-4) The name, address, telephone number (including area code), facsimile number (including area code), and E-mail address of the Applicant's Management Contact:

Jon Brinton, President
4310 East Cotton Center Blvd., Suite A-100
Phoenix, Arizona 85040
Telephone: (602) 253-6004
Fax: (602) 532-4128
E-Mail Address: jon_brinton@inter-tel.com

(A-5) The name, address, telephone number (including area code), facsimile number (including area code), and E-mail address of the Applicant's Attorney and/or Consultant:

Lance J.M. Steinhart, Esq.
Lance J.M. Steinhart, P.C.
1720 Windward Concourse, Suite 250
Alpharetta, Georgia 30005
Telephone: (770) 232-9200
Fax: (770) 232-9208
E-Mail Address: lsteinhart@telecomcounsel.com

(A-6) The name, address, telephone number (including area code), facsimile number (including area code), E-mail address of the Applicant's Complaint Contact Person:

Allison Dunmire, Customer Service Manager
4310 East Cotton Center Blvd., Suite A-100
Phoenix, Arizona 85040
Telephone: (602) 253-6004
Fax: (602) 532-4128
E-Mail Address: Allison_Dunmire@inter-tel.com

(A-7) What type of legal entity is the Applicant?

☐ Sole proprietorship

☐ Partnership: _____ Limited, _____ General, _____ Arizona, _____ Foreign

☐ Limited Liability Company: _____ Arizona, _____ Foreign

☒ Corporation: _____ "S", _____ "C", _____ Non-profit

☒ Domicile: _____ Arizona, __X__ Foreign

☐ Other, specify: ______

(A-8) Please include "Attachment A":

Attachment "A" <u>must</u> include the following information:

1. A copy of the Applicant's Certificate of Good Standing as a domestic or foreign corporation, LLC, or other entity in the State of Arizona.
2. A list of the names of all owners, partners, limited liability company managers (or if a member managed LLC, all members), or corporation officers and directors (specify).
3. Indicate percentages of ownership of each person listed in A-8.2.

(A-9) Include your Tariff as "Attachment B".

Your Tariff must include the following information:

1. Proposed Rates and Charges for each service offered (reference by Tariff page number).

   See Sheets 103 - 119 of the Company's Tariff.

2. Tariff Maximum Rate and Prices to be charged (reference by Tariff page number).

   See Sheets 57 - 99 of the Company's Tariff.

3. Terms and Conditions Applicable to provision of Service (reference by Tariff page number).

   See Sheets 11 – 56 of the Company's Tariff.

4. Deposits, Advances, and/or Prepayments Applicable to provision of Service (reference by Tariff page number).

   See Sheets 32 and 33 of the Company's Tariff.

5. The proposed fee that will be charged for returned checks (reference by Tariff page number).

   See Sheet 31 of the Company's Tariff.

(A-10) Indicate the geographic market to be served:

☒ Statewide. (Applicant adopts statewide map of Arizona provided with this application).

☐ Other. Describe and provide a detailed map depicting the area.

(A-11) Indicate if the Applicant or any of its officers, directors, partners, or managers has been or are currently involved in any formal or informal complaint proceedings pending before any state or federal regulatory commission, administrative agency, or law enforcement agency.

Describe in detail any such involvement. Please make sure you provide the following information:

1. States in which the Applicant has been or is involved in proceedings.
2. Detailed explanations of the Substance of the Complaints.
3. Commission Orders that resolved any and all Complaints.
4. Actions taken by the Applicant to remedy and/or prevent the Complaints from re-occurring.

Neither Applicant nor any of its officers, directors, partners, or managers has been or are currently involved in any formal or informal complaint proceedings pending before any state or federal regulatory commission, administrative agency, or law enforcement agency.

(A-12) Indicate if the Applicant or any of its officers, directors, partners, or managers has been or are currently involved in any civil or criminal investigation, or had judgments entered in any civil matter, judgments levied by any administrative or regulatory agency, or been convicted of any criminal acts within the last ten (10) years.

Describe in detail any such judgments or convictions. Please make sure you provide the following information:

1. States involved in the judgments and/or convictions.
2. Reasons for the investigation and/or judgment.
3. Copy of the Court order, if applicable.

Neither Applicant nor any of its officers, directors, partners, or managers has been or are currently involved in any civil or criminal investigation, or had judgments entered in any civil matter, judgments levied by any administrative or regulatory agency, or been convicted of any criminal acts within the last ten (10) years.

(A-13) Indicate if the Applicant's customers will be able to access alternative toll service providers or resellers via 1+101XXXX access.

☒ Yes ☐ No

(A-14) Is applicant willing to post a Performance Bond? Please check appropriate box(s).

☐ For Long Distance Resellers, a $10,000 bond will be recommended for those resellers who collect advances, prepayments or deposits.

☐ Yes ☐ No

If "No", continue to question (A-15).

☒ For Local Exchange Resellers, a $25,000 bond will be recommended.

☒ Yes ☐ No

If "No", continue to question (A-15).

☐ For Facilities-Based Providers of Long Distance, a $100,000 bond will be recommended.

☐ Yes ☐ No

If "No", continue to question (A-15).

☐ For Facilities-Based Providers of Local Exchange, a $100,000 bond will be recommended.

☐ Yes ☐ No

If "No", continue to question (A-15).

Note: Amounts are cumulative if the Applicant is applying for more than one type of service.

(A-15) If No to any of the above, provide the following information. Clarify and explain the Applicant's deposit policy (reference by tariff page number). Provide a detailed explanation of why the applicant's superior financial position limits any risk to Arizona consumers.

(A-16) Submit copies of affidavits of publication that the Applicant has, as required, published legal notice of the Application in all counties where the applicant is requesting authority to provide service.

Note: For Resellers, the Applicant must complete and submit an Affidavit of Publication Form as Attachment "C" before Staff prepares and issues its report. Refer to the Commission's website for Legal Notice Material (Newspaper Information, Sample Legal Notice and Affidavit of Publication). For Facilities-Based Service Providers, the Hearing Division will advise the Applicant of the date of the hearing and the publication of legal notice. Do not publish legal notice or file affidavits of publication until your are advised to do so by the Hearing Division.

(A-17) Indicate if the Applicant is a switchless reseller of the type of telecommunications services that the Applicant will or intends to resell in the State of Arizona:

☒ Yes ☐ No

If "Yes", provide the name of the company or companies whose telecommunications services the Applicant resells.

The company intends to resell services provided by AT&T, MCI and XO

(A-18) List the States in which the Applicant has had an application approved or denied to offer telecommunications services similar to those that the Applicant will or intends to offer in the State of Arizona:

Note: If the Applicant is currently approved to provide telecommunications services that the Applicant intends to provide in Arizona in less than six states, excluding Arizona, list the Public Utility Commission ("PUC") of each state that granted the authorization. For each PUC listed provide the name of the contact person, their phone number, mailing address including zip code, and e-mail address.

Approved: **The applicant is authorized to provide long distance service throughout the United States.**

(A-19) List the States in which the Applicant currently offers telecommunications services similar to those that the Applicant will or intends to offer in the State of Arizona.

Note: If the Applicant currently provides telecommunication services that the Applicant intends to provide in Arizona in six or more states, excluding Arizona, list the states. If the Applicant does not currently provide telecommunications services that the Applicant intends to provide in Arizona in five or less states, list the key personnel employed by the Applicant. Indicate each employee's name, title, position, description of their work experience, and years of service in the telecommunications services industry.

The applicant is authorized to provide local exchange service in Colorado, Georgia, Illinois, Missouri, New Jersey, New York and Texas.

(A-20) List the names and addresses of any alternative providers of the service that are also affiliates of the telecommunications company, as defined in R14-2-801.

None.

B. FINANCIAL INFORMATION

(B-1) Indicate if the Applicant has financial statements for the two (2) most recent years.

☒ Yes ☐ No

If "No," explain why and give the date on which the Applicant began operations.

(B-2) Include "Attachment D".

Provide the Applicant's financial information for the two (2) most recent years.

1. A copy of the Applicant's balance sheet.
2. A copy of the Applicant's income statement.
3. A copy of the Applicant's audit report.
4. A copy of the Applicant's retained earnings balance.
5. A copy of all related notes to the financial statements and information.

Note: Make sure "most recent years" includes current calendar year or current year reporting period.

(B-3) Indicate if the Applicant will rely on the financial resources of its Parent Company, if applicable.

Yes.

(B-4) The Applicant must provide the following information.

1. Provide the projected total revenue expected to be generated by the provision of telecommunications services to Arizona customers for the first twelve months following certification, adjusted to reflect the maximum rates for which the Applicant requested approval. Adjusted revenues may be calculated as the number of units sold times the maximum charge per unit.
2. Provide the operating expenses expected to be incurred during the first twelve months of providing telecommunications services to Arizona customers following certification.
3. Provide the net book value (original cost less accumulated depreciation) of all Arizona jurisdictional assets expected to be used in the provision of telecommunications service to Arizona customers at the end of the first twelve months of operation. Assets are not limited to plant and equipment. Items such as office equipment and office supplies should be included in this list.
4. If the projected value of all assets is zero, please specifically state this in your response.
5. If the projected fair value of the assets is different than the projected net book value, also provide the corresponding projected fair value amounts.

See "Attachment E"

C. RESOLD AND/OR FACILITIES-BASED LOCAL EXCHANGE TELECOMMUNICATIONS SERVICES

(C-1) Indicate if the Applicant has a resale agreement in operation,

☐ Yes ☒ No

If "Yes", please reference the resale agreement by Commission Docket Number or Commission Decision Number.

D. FACILITIES-BASED LONG DISTANCE AND/OR FACILITIES BASED LOCAL EXCHANGE TELECOMMUNICATIONS SERVICES

(D-1) Indicate if the Applicant is currently selling facilities-based long distance telecommunications services AND/OR facilities-based local exchange telecommunications services in the State of Arizona. This item applies to an Applicant requesting a geographic expansion of their CC&N:

☐ Yes ☒ No

If "Yes," provide the following information:

1. The date or approximate date that the Applicant began selling facilities-based long distance telecommunications services AND/OR facilities-based local exchange telecommunications services for the State of Arizona.

2. Identify the types of facilities-based long distance telecommunications services AND/OR facilities-based local exchange telecommunications services that the Applicant sells in the State of Arizona.

If "No," indicate the date when the Applicant will begin to sell facilities-based long distance telecommunications AND/OR facilities-based local exchange telecommunications services in the State of Arizona:

(D-2) Check here if you wish to adopt as your petition a statement that the service has already been classified as competitive by Commission Decision:

- ☐ Decision # 64178 Resold Long Distance
- ☒ Decision # 64178 Resold LEC
- ☐ Decision # 64178 Facilities Based Long Distance
- ☐ Decision # 64178 Facilities Based LEC

E. FACILITIES-BASED LOCAL EXCHANGE TELECOMMUNICATIONS SERVICES

(E-1) Indicate whether the Applicant will abide by the quality of service standards that were approved by the Commission in Commission Decision Number 59241:

☐ Yes ☐ No

(E-2) Indicate whether the Applicant will provide all customers with 911 and E911 service, where available, and will coordinate with incumbent local exchange carriers ("ILECs") and emergency service providers to provide this service:

☐ Yes ☐ No

(E-3) Indicate that the Applicant's switch is "fully equal access capable" (i.e., would provide equal access to facilities-based long distance companies) pursuant to A.A.C. R14-2-1111 (A):

☐ Yes ☐ No

I certify that if the applicant is an Arizona corporation, a current copy of the Certificate of Incorporation is on file with the Arizona Corporation Commission and the applicant holds a Certificate of Good Standing from the Commission. If the company is a foreign corporation or partnership, I certify that the company has authority to transact business in Arizona. I certify that all appropriate city, county and/or State agency approvals have been obtained. Upon signing of this application I attest that I have read the Commission's rules and regulations relating to the regulations of telecommunications services and that the company will abide by Arizona State Law including the Arizona Corporation Commission Rules and Regulations. I agree that the Commission's rules apply in the event there is a conflict between those rules and the company's tariff, unless otherwise ordered by the Commission. I certify that to the best of my knowledge the information provided in this Application and Petition is true and correct.

Jon Brinton
President

Date: 9/1/2005

SUBSCRIBED AND SWORN to before me this 1 day of September, 2005.

Lori Prigge
NOTARY PUBLIC

My Commission Expires: 8/12/06

OFFICIAL SEAL
LORI PRIGGE
NOTARY PUBLIC - STATE OF ARIZONA
MARICOPA COUNTY
My Commission Expires Aug. 12, 2006

ATTACHMENTS

A – Certificate of Good Standing, List of Officers and Directors or Owners and Percentage of Ownership

B - Proposed Tariff

C - Legal Notice

D - Financial Information

E - Arizona Projections

A - Certificate of Good Standing and

Officers, Directors and Owners	**Percentage Ownership**
Officers:	
Jon Brinton, President	
Steven G. Mihaylo, Vice President	
Kurt R. Kneip, Vice President & Secretary	
John C. Abbott, Treasurer	
Todd West, Vice President, Operations	
Allison Dunmire, Manager of Provisioning & Customer Service	
Doug Milliron, Manager of Dedicated & Managed Services	
Holly Thomas, Controller	
Directors:	
Ross E. McAlpine Director	
Steven G. Mihaylo Director	
Kurt R. Kneip Director	
Owners:	
Inter-Tel, Inc.	100%

B - Proposed Tariff

Arizona

LOCAL EXCHANGE TELECOMMUNICATIONS SERVICES TARIFF

OF

Inter-Tel NetSolutions, Inc.

This tariff contains the descriptions, regulations, and rates applicable to the provision of local exchange telecommunications services provided by Inter-Tel NetSolutions, Inc. with principal offices at4310 East Cotton Center Blvd., Suite A-100, Phoenix, Arizona 85040 for services furnished within the State of Arizona. This tariff is on file with the Arizona Corporation Commission, and copies may be inspected, during normal business hours, at the Company's principal place of business.

TABLE OF CONTENTS

CHECK SHEET

Pages of this tariff are effective as of the date shown at the bottom of the respective page(s). Original and revised pages as named below comprise all changes from the original tariff and are currently in effect as of the date on the bottom of this page.

SECTION	PAGE	REVISION	SECTION	PAGE	REVISION
Preface	1	Original	2	31	Original
Preface	2	Original	2	32	Original
Preface	3	Original	2	33	Original
Preface	4	Original	2	34	Original
Preface	5	Original	2	35	Original
Preface	6	Original	2	36	Original
1	7	Original	2	37	Original
1	8	Original	2	38	Original
1	9	Original	2	39	Original
1	10	Original	2	40	Original
2	11	Original	2	41	Original
2	12	Original	2	42	Original
2	13	Original	2	43	Original
2	14	Original	2	44	Original
2	15	Original	2	45	Original
2	16	Original	2	46	Original
2	17	Original	2	47	Original
2	18	Original	2	48	Original
2	19	Original	2	49	Original
2	20	Original	3	50	Original
2	21	Original	4	51	Original
2	22	Original	4	52	Original
2	23	Original	4	53	Original
2	24	Original	4	54	Original
2	25	Original	4	55	Original
2	26	Original	4	56	Original
2	27	Original	4	57	Original
2	28	Original	4	58	Original
2	29	Original	4	59	Original
2	30	Original	4	60	Original

CHECK SHEET, (CONT'D.)

Pages of this tariff are effective as of the date shown at the bottom of the respective page(s). Original and revised pages as named below comprise all changes from the original tariff and are currently in effect as of the date on the bottom of this page.

SECTION	PAGE	REVISION	SECTION	PAGE	REVISION	SECTION	PAGE	REVISION
4	61	Original	5	93	Original	10	120	Original
4	62	Original	5	94	Original	10	121	Original
4	63	Original	5	95	Original	10	122	Original
4	64	Original	5	96	Original	10	123	Original
4	65	Original	5	97	Original	10	124	Original
4	66	Original	5	98	Original	10	125	Original
4	67	Original	5	99	Original	10	126	Original
4	68	Original	5	100	Original	10	127	Original
5	69	Original	5	101	Original	10	128	Original
5	70	Original	5	102	Original	10	129	Original
5	71	Original	5	103	Original			
5	72	Original	5	104	Original			
5	73	Original	6	105	Original			
5	74	Original	7	106	Original			
5	75	Original	7	107	Original			
5	76	Original	7	108	Original			
5	77	Original	7	109	Original			
5	78	Original	7	110	Original			
5	79	Original	7	111	Original			
5	80	Original	7	112	Original			
5	81	Original	7	113	Original			
5	82	Original	7	114	Original			
5	83	Original	8	115	Original			
5	84	Original	9	116	Original			
5	85	Original	10	117	Original			
5	86	Original	10	118	Original			
5	87	Original	10	119	Original			
5	88	Original						
5	89	Original						
5	90	Original						
5	91	Original						
5	92	Original						

EXPLANATION OF SYMBOLS, REFERENCE MARKS, AND ABBREVIATIONS OF TECHNICAL TERMS USED IN THIS TARIFF

The following symbols shall be used in this tariff for the purpose indicated below:

(C) To signify changed regulation.
(D) To signify discontinued rate or regulation.
(I) To signify increased rate.
(M) To signify a move in the location of text.
(N) To signify new rate or regulation.
(R) To signify reduced rate.
(S) To signify reissued matter.
(T) To signify a change in text but no change in rate or regulation.

APPLICATION OF TARIFF

This tariff sets forth the service offerings, rates, terms and conditions applicable to the furnishing of intrastate end-user local exchange communications services by Inter-Tel NetSolutions, Inc., hereinafter referred to as the Company, to Customers within the state of Arizona. Inter-Tel's services are furnished subject to the availability of facilities and subject to the terms and conditions set forth herein.

This tariff is on file with the Arizona Corporation Commission. In addition, this tariff is available for review at the main office of Inter-Tel NetSolutions, Inc. at4310 East Cotton Center Blvd., Suite A-100, Phoenix, Arizona 85040.

TARIFF FORMAT

A. **Page Numbering** - Page numbers appear in the upper right corner of the page. Pages are numbered sequentially. However, new pages are occasionally added to the tariff. When a new page is added between pages already in effect, a decimal is added. For example, a new page added between pages 14 and 15 would be 14.1.

B. **Page Revision Numbers** - Revision numbers also appear in the upper right corner of each page. These numbers are used to determine the most current page version on file with the Commission. For example, the 4th revised Page 14 cancels the 3rd revised Page 14. Because of various suspension periods, deferrals, etc., the most current page number on file with the Commission is not always the tariff page in effect. Consult the Check Sheet for the page currently in effect.

C. **Paragraph Numbering Sequence** - There are nine levels of paragraph coding. Each level of coding is subservient to its next higher level:

2.
2.1.
2.1.1.
2.1.1.A.
2.1.1.A.1.
2.1.1.A.1.(a).
2.1.1.A.1.(a).I.
2.1.1.A.1.(a).I.(i).
2.1.1.A.1.(a).I.(i).(1).

D. **Check Sheets** - When a tariff filing is made with the Commission, an updated Check Sheet accompanies the tariff filing. The Check Sheet lists the pages contained in the tariff, with a cross reference to the current revision number. When new pages are added, the Check Sheet is changed to reflect the revision. All revisions made in a given filing are designated by an asterisk (*). There will be no other symbols used on this page if these are the only changes made to it (i.e., the format, etc. remain the same, just revised revision levels on some pages.) The tariff user should refer to the latest Check Sheet to find out if a particular page is the most current on file with the Commission.

SECTION 1.0 – DEFINITIONS

Access Line - An arrangement from a local exchange telephone company or other common carrier, using either dedicated or switched access, which connects a Customer's location to Carrier's location or switching center.

Account - A Company accounting category containing up to two (2) residential local exchange access lines billed to the same Customer at the same address. The second or non-primary local exchange access line will share any call allowance of the primary local exchange access line. The second or non-primary local exchange access line therefore will not be provisioned to include a separate call allowance structure. No features are included with the second or non-primary local exchange access line.

Account Codes - Permits Centrex Stations and attendants to dial an account code number of up to eight digits. For use when placing calls over facilities arranged for Automatic Message Accounting (AMA) recording. The account or project number must be input prior to dialing the called number.

Advance Payment - Part or all of a payment required before the start of service.

Authorization Code - A numerical code, one or more of which may be assigned to a Customer, to enable Carrier to identify the origin of service of the Customer so it may rate and bill the call. All authorization codes shall be the sole property of Carrier and no Customer shall have any property or other right or interest in the use of any particular authorization code. Automatic numbering identification (ANI) may be used as or in connection with the authorization code.

Authorized User - A person, firm or corporation authorized by the Customer to be an end-user of the service of the Customer.

Automatic Numbering Identification (ANI) - A type of signaling provided by a local exchange telephone company which automatically identifies the local exchange line from which a call originates.

Commission - Arizona Corporation Commission.

Common Carrier - An authorized company or entity providing telecommunications services to the public

Company -Inter-Tel NetSolutions, Inc., the issuer of this tariff.

Customer - The person, firm or corporation that orders service and is responsible for the payment of charges and compliance with the terms and conditions of this tariff.

Customer Premises - A location designated by the Customer for the purposes of connecting to the Company's services.

Customer Terminal Equipment - Terminal equipment provided by the Customer.

SECTION 1.0 - DEFINITIONS, (CONT'D.)

Deposit - Refers to a cash or equivalent of cash security held as a guarantee for payment of the charges.

End Office - The LEC switching system office or serving wire center where Customer station loops are terminated for purposes of interconnection to each other and/or to trunks.

Equal Access - A form of dialed access provided by local exchange companies whereby interexchange calls dialed by the Customer are automatically routed to the Company's network. Presubscribed Customers may also route interexchange calls to the Company's network by dialing an access code supplied by the Company.

Exchange Telephone Company or Telephone Company - Denotes any individual, partnership, association, joint-stock company, trust, or corporation authorized by the appropriate regulatory bodies to engage in providing public switched communication service throughout an exchange area, and between exchange areas within the LATA.

ICB - Individual Case Basis.

IXC or Interexchange Carrier- A long distance telecommunications services provider.

Interruption - The inability to complete calls due to equipment malfunctions or human errors. Interruption shall not include, and no allowance shall be given for service difficulties such as slow dial tone, circuits busy or other network and/or switching capability shortages. Nor shall Interruption include the failure of any service or facilities provided by a common carrier or other entity other than the Carrier. Any Interruption allowance provided within this Tariff by Carrier shall not apply where service is interrupted by the negligence or willful act of the Customer, or where the Carrier, pursuant to the terms of this Tariff, terminates service because of non-payment of bills, unlawful or improper use of the Carrier's facilities or service, or any other reason covered by this Tariff or by applicable law.

LATA - A Local Access and Transport Area established pursuant to the Modification of Final Judgment entered by the United States District Court for the District of Columbia in Civil Action No. 82-0192; or any other geographic area designated as a LATA in the National Exchange Carrier Association, Inc. Tariff F.C.C. No. 4, or its successor tariff(s).

LEC - Local Exchange Company refers to the dominant, monopoly local telephone company in the area also served by the Company.

SECTION 1.0 - DEFINITIONS, (CONT'D.)

Monthly Recurring Charges - The monthly charges to the Customer for services, facilities and equipment, which continue for the agreed upon duration of the service.

MOU - Minutes of Use.

NECA - National Exchange Carriers Association.

Non-Recurring Charge ("NRC") - The initial charge, usually assessed on a one-time basis, to initiate and establish service.

PBX - Private Branch Exchange

PIN - Personal Identification Number. See Authorization Code.

Point of Presence ("POP") - Point of Presence

Recurring Charges - Monthly charges to the Customer for services, and equipment, which continues for the agreed upon duration of the service.

Service - Any means of service offered herein or any combination thereof.

Service Order - The written request for Company services executed by the Customer and the Company in the format devised by the Company. The signing of a Service Order Form by the Customer and acceptance by the Company initiates the respective obligations of the parties as set forth therein and pursuant to this tariff.

Serving Wire Center - A specified geographic point from which the vertical and horizontal coordinate is used in calculation of airline mileage.

Shared Inbound Calls - Refers to calls that are terminated via the Customer's Company-provided local exchange line.

Shared Outbound Calls - Refers to calls in Feature Group (FGD) exchanges whereby the Customer's local telephone lines are presubscribed by the Company to the Company's outbound service such that "1 + 10-digit number" calls are automatically routed to the Company's or an IXC's network. Calls to stations within the Customer's LATA may be placed by dialing "10XXX" or "101XXXX" with 1 + 10-digit number."

SECTION 1.0 - DEFINITIONS, (CONT'D.)

Station - The network control signaling unit and any other equipment provided at the Customer's premises which enables the Customer to establish communications connections and to effect communications through such connections.

Subscriber - The person, firm, partnership, corporation, or other entity who orders telecommunications service from Inter-Tel. Service may be ordered by, or on behalf of, those who own, lease or otherwise manage the pay telephone, PBX, or other switch vehicle from which an End User places a call utilizing the services of the Company.

Switched Access Origination/Termination - Where access between the Customer and the interexchange carrier is provided on local exchange company Feature Group circuits and the connection to the Customer is a LED-provided business or residential access line. The cost of switched Feature Group access is billed to the interexchange carrier.

Terminal Equipment - Any telecommunications equipment other than the transmission or receiving equipment installed at a Company location.

Usage Charges - Charges for minutes or messages traversing over local exchange facilities.

User or End User - A Customer, Joint User, or any other person authorized by a Customer to use service provided under this tariff.

SECTION 2.0 - REGULATIONS

2.1 Undertaking of the Company

2.1.1 Scope

The Company undertakes to furnish communications service pursuant to the terms of this tariff in connection with one-way and/or two-way information transmission between points within the state of Arizona.

The Company is responsible under this tariff only for the services and facilities provided hereunder, and it assumes no responsibility for any service provided by any other entity that purchases access to the Company network in order to originate or terminate its own services, or to communicate with its own customers.

2.1.2 Shortage of Equipment or Facilities

2.1.2.A. The Company reserves the right to limit or to allocate the use of existing facilities, or of additional facilities offered by the Company, when necessary because of lack of facilities, or due to some other cause beyond the Company's control.

2.1.2.B. The furnishing of service under this tariff is subject to the availability on a continuing basis of all the necessary facilities and is limited to the capacity of the Company's facilities as well as facilities the Company may obtain from other carriers to furnish service from time to time as required at the sole discretion of the Company.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.3 Terms and Conditions

2.1.3.A. Service is provided on the basis of a minimum period of at least thirty (30) days, 24-hours per day. For the purpose of computing charges in this tariff, a month is considered to have 30 days.

2.1.3.B. Except as otherwise stated in this tariff, Customers may be required to enter into written service orders which shall contain or reference a specific description of the service ordered, the rates to be charged, the duration of the services, and the terms and conditions in this tariff. Customers will also be required to execute any other documents as may be reasonably requested by the Company.

2.1.3.C. At the expiration of the initial term specified in each Service Order, or in any extension thereof, service shall continue on a month-to-month basis at the then current rates unless terminated by either party upon notice. Any termination shall not relieve the Customer of its obligation to pay any charges incurred under the service order and this tariff prior to termination. The rights and obligations which by their nature extend beyond the termination of the term of the service order shall survive such termination.

2.1.3.D. In any action between the parties to enforce any provision of this tariff, the prevailing party shall be entitled to recover its legal fees and court costs from the non-prevailing party in addition to other relief a court may award.

2.1.3.E. Service may be terminated upon written notice to the Customer if:

2.1.3.E.1 the Customer is using the service in violation of this tariff; or

2.1.3.E.2 the Customer is using the service in violation of the law.

2.1.3.F. This tariff shall be interpreted and governed by the laws of the state of Arizona regardless of its choice of laws provision.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.3 Terms and Conditions, (Cont'd.)

2.1.3.G. Any other Telephone Company may not interfere with the right of any person or entity to obtain service directly from the Company. No person or entity shall be required to make any payment, incur any penalty, monetary or otherwise, or purchase any services in order to have the right to obtain service directly from the Company.

2.1.3.H. To the extent that either the Company or any other telephone company exercises control over available cable pairs, conduit, duct space, raceways, or other facilities needed by the other to reach a person or entity, the party exercising such control shall make them available to the other on terms equivalent to those under which the Company makes similar facilities under its control available to its customers. At the reasonable request of either party, the Company and the other telephone company shall join the attempt to obtain from the owner of the property access for the other party to serve a person or entity.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Limitations on Liability

2.1.4.A. Except as otherwise stated in this section, the liability of the Company for damages arising out of either: (1) the furnishing of its services, including but not limited to mistakes, omissions, interruptions, delays, or errors, or other defects, representations, or use of these services or (2) the failure to furnish its service, whether caused by acts or omission, shall be limited to the extension of allowances to the Customer for interruptions in service as set forth in Section 2.6.

2.1.4.B. Except for the extension of allowances to the Customer for interruptions in service as set forth in Section 2.6, the Company shall not be liable to a Customer or third party for any direct, indirect, special, incidental, reliance, consequential, exemplary or punitive damages, including, but not limited to, loss of revenue or profits, for any reason whatsoever, including, but not limited to, any act or omission, failure to perform, delay, interruption, failure to provide any service or any failure in or breakdown of facilities associated with the service.

2.1.4.C. The liability of the Company for errors in billing that result in overpayment by the Customer shall be limited to a credit equal to the dollar amount erroneously billed or, in the event that payment has been made and service has been discontinued, to a refund of the amount erroneously billed.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Limitations on Liability, (Cont'd.)

2.1.4.D. The Company shall be indemnified and saved harmless by the Customer from and against all loss, liability, damage and expense, including reasonable counsel fees, due to:

2.1.4.D.1 Any act or omission of: (a) the Customer, (b) any other entity furnishing service, equipment or facilities for use in conjunction with services or facilities provided by the Company; or (c) common carriers or warehousemen, except as contracted by the Company;

2.1.4.D.2 Any delay or failure of performance or equipment due to causes beyond the Company's control, including but not limited to, acts of God, fires, floods, earthquakes, hurricanes, or other catastrophes; national emergencies, insurrections, riots, wars or other civil commotions; strikes, lockouts, work stoppages or other labor difficulties; criminal actions taken against the Company; unavailability, failure or malfunction of equipment or facilities provided by the Customer or third parties; and any law, order, regulation or other action of any governing authority or agency thereof;

2.1.4.D.3 Any unlawful or unauthorized use of the Company's facilities and services;

2.1.4.D.4 Libel, slander, invasion of privacy or infringement of patents, trade secrets, or copyrights arising from or in connection with the material transmitted by means of Company-provided facilities or services; or by means of the combination of Company-provided facilities or services;

2.1.4.D.5 Breach in the privacy or security of communications transmitted over the Company's facilities;

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Limitations on Liability, (Cont'd.)

2.1.4.D. (Cont'd.)

2.1.4.D.6 Changes in any of the facilities, operations or procedures of the Company that render any equipment, facilities or services provided by the Customer obsolete, or require modification or alteration of such equipment, facilities or services, or otherwise affect their use or performance, except where reasonable notice is required by the Company and is not provided to the Customer, in which event the Company's liability is limited as set forth in paragraph A. of this Subsection 2.1.4.

2.1.4.D.7 Defacement of or damage to Customer premises resulting from the furnishing of services or equipment on such premises or the installation or removal thereof;

2.1.4.D.8 Injury to property or injury or death to persons, including claims for payments made under Workers' Compensation law or under any plan for employee disability or death benefits, arising out of, or caused by, any act or omission of the Customer, or the construction, installation, maintenance, presence, use or removal of the Customer's facilities or equipment connected, or to be connected to the Company's facilities;

2.1.4.D.9 Any noncompletion of calls due to network busy conditions;

2.1.4.D.10 Any calls not actually attempted to be completed during any period that service is unavailable;

2.1.4.D.11 And any other claim resulting from any act or omission of the Customer or patron(s) of the Customer relating to the use of the Company's services or facilities.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Limitations on Liability, (Cont'd.)

2.1.4.E. The Company does not guarantee nor make any warranty with respect to installations provided by it for use in an explosive atmosphere.

2.1.4.F. The Company makes no warranties or representations, EXPRESS OR IMPLIED, either in fact or by operation of law, statutory or otherwise, including warranties of merchantability or fitness for a particular use, except those expressly set forth herein.

2.1.4.G. Failure by the Company to assert its rights pursuant to one provision of this rate sheet does not preclude the Company from asserting its rights under other provisions.

2.1.4.H. Directory Errors - In the absence of gross negligence or willful misconduct, no liability for damages arising from errors or mistakes in or omissions of directory listings, or errors or mistakes in or omissions of listing obtainable from the directory assistance operator, including errors in the reporting thereof, shall attach to the Company. An allowance for errors or mistakes in or omissions of published directory listings or for errors or mistakes in or omissions of listing obtainable from the directory assistance operator shall be at the monthly tariff rate for each listing, or in the case of a free or no-charge directory listing, credit shall equal two times the monthly tariff rate for an additional listing, for the life of the directory or the charge period during which the error, mistake or omission occurs.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Limitations on Liability, (Cont'd.)

2.1.4.I. With respect to Emergency Number 911 Service:

2.1.4.I.1 This service is offered solely as an aid in handling assistance calls in connection with fire, police and other emergencies. The Company is not responsible for any losses, claims, demands, suits or any liability whatsoever, whether suffered, made instituted or asserted by the Customer or by any other party or person for any personal injury or death of any person or persons, and for any loss, damage or destruction of any property, whether owned by the Customer or others, caused or claimed to have been caused by: (1) mistakes, omissions, interruptions, delays, errors or other defects in the provision of service, or (2) installation, operation, failure to operate, maintenance, removal, presence, condition, local or use of any equipment and facilities furnishing this service.

2.1.4.I.2 Neither is the Company responsible for any infringement, nor invasion of the right of privacy of any person or persons, caused or claimed to have been caused directly or indirectly, by the installation, operation, failure to operate, maintenance, removal, presence, condition, occasion or use of emergency 911 service features and the equipment associated therewith, or by any services furnished by the Company, including, but not limited to the identification of the telephone number, address or name associated with the telephone used by the party or parties accessing emergency 911 service, and which arise out of the negligence or other wrongful act of the Company, the Customer, its users, agencies or municipalities, or the employees or agents of any one of them.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.4 Limitations on Liability, (Cont'd.)

2.1.4.I. With respect to Emergency Number 911 Service, (Cont'd.)

2.1.4.I.3 When a Customer with a nonpublished telephone number, as defined herein, places a call to the emergency 911 service, the Company will release the name and address of the calling party, where such information can be determined, to the appropriate local governmental authority responsible for emergency 911 service upon request of such governmental authority. By subscribing to service under this rate sheet, the Customer acknowledges and agrees with the release of information as described above.

2.1.5 Notification of Service-Affecting Activities

The Company will provide the Customer reasonable notification of service-affecting activities that may occur in normal operation of its business. Such activities may include, but are not limited to, equipment or facilities additions, removals or rearrangements and routine preventative maintenance. Generally, such activities are not specific to an individual Customer but affect many Customers' services. No specific advance notification period is applicable to all service activities. The Company will work cooperatively with the Customer to determine the reasonable notification requirements. With some emergency or unplanned service-affecting conditions, such as an outage resulting from cable damage, notification to the Customer may not be possible.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.6 Provision of Equipment and Facilities

2.1.6.A. The Company shall use reasonable efforts to make available services to a Customer on or before a particular date, subject to the provisions of and compliance by the Customer with, the regulations contained in this tariff. The Company does not guarantee availability by any such date and shall not be liable for any delays in commencing service to any Customer.

2.1.6.B. The Company shall use reasonable efforts to maintain only the facilities and equipment that it furnishes to the Customer. The Customer may not, nor may the Customer permit others to, rearrange, disconnect, remove, attempt to repair, or otherwise interfere with any of the facilities or equipment installed by the Company, except upon the written consent of the Company.

2.1.6.C. The Company may substitute, change or rearrange any equipment or facility at any time and from time to time, but shall not thereby alter the technical parameters of the service provided the Customer.

2.1.6.D. Equipment the Company provides or installs at the Customer Premises for use in connection with the services the Company offers shall not be used for any purpose other than that for which it was provided.

2.1.6.E. The Customer shall be responsible for the payment of service charges as set forth herein for visits by the Company's agents or employees to the Premises of the Customer when the service difficulty or trouble report results from the use of equipment or facilities provided by any party other than the Company, including but not limited to the Customer.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.6 Provision of Equipment and Facilities, (Cont'd.)

2.1.6.F. The Company shall not be responsible for the installation, operation, or maintenance of any Customer-provided communications equipment. Where such equipment is connected to the facilities furnished pursuant to this tariff, the responsibility of the Company shall be limited to the furnishing of facilities offered under this tariff and to the maintenance and operation of such facilities. Subject to this responsibility, the Company shall not be responsible for:

(1) the transmission of signals by Customer-provided equipment or for the quality of, or defects in, such transmission; or

(2) the reception of signals by Customer-provided equipment.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.1 Undertaking of the Company, (Cont'd.)

2.1.7 Non-routine Installation

At the Customer's request, installation and/or maintenance may be performed outside the Company's regular business hours or in hazardous locations. In such cases, charges based on cost of the actual labor, material, or other costs incurred by or charged to the Company will apply. If installation is started during regular business hours but, at the Customer's request, extends beyond regular business hours into time periods including, but not limited to, weekends, holidays, and/or night hours, additional charges may apply.

2.1.8 Special Construction

Subject to the agreement of the Company and to all of the regulations contained in this tariff, special construction of facilities may be undertaken on a reasonable efforts basis at the request of the Customer. Special construction is that construction undertaken:

A. where facilities are not presently available, and there is no other requirement for the facilities so constructed;

B. of a type other than that which the Company would normally utilize in the furnishing of its services;

C. over a route other than that which the Company would normally utilize in the furnishing of its services;

D. in a quantity greater than that which the Company would normally construct;

E. on an expedited basis;

F. on a temporary basis until permanent facilities are available;

G. involving abnormal costs; or

H. in advance of its normal construction.

2.1.9 Ownership of Facilities

Title to all facilities provided in accordance with this rate sheet remains in the Company, its partners, agents, contractors or suppliers.

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President
4310 East Cotton Center Blvd., Suite A-100
Phoenix, Arizona 85040

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.2 Prohibited Uses

2.2.1 The services the Company offers shall not be used for any unlawful purpose or for any use as to which the Customer has not obtained all required governmental approvals, authorizations, licenses, consents and permits.

2.2.2 The Company may require applicants for service who intend to use the Company's offerings for resale and/or for shared use to file a letter with the Company confirming that their use of the Company's offerings complies with relevant laws and Commission regulations, policies, orders, and decisions.

2.2.3 The Company may block any signals being transmitted over its Network by Customers which cause interference to the Company or other users. Customer shall be relieved of all obligations to make payments for charges relating to any blocked Service and shall indemnify the Company for any claim, judgment or liability resulting from such blockage.

2.2.4 A customer, joint user, or authorized user may not assign, or transfer in any manner, the service or any rights associated with the service without the written consent of the Company. The Company will permit a Customer to transfer its existing service to another entity if the existing Customer has paid all charges owed to the Company for regulated communications services. Such a transfer will be treated as a disconnection of existing service and installation of new service, and non-recurring installation charges as stated in this tariff will apply.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.3 Obligations of the Customer

2.3.1 General

The Customer is responsible for making proper application for service; placing any necessary order, complying with tariff regulations; payment of charges for services provided. Specific Customer responsibilities include, but are not limited to the following:

A. the payment of all applicable charges pursuant to this tariff;

B. damage to or loss of the Company's facilities or equipment caused by the acts or omissions of the Customer; or the noncompliance by the Customer, with these regulations; or by fire or theft or other casualty on the Customer Premises, unless caused by the negligence or willful misconduct of the employees or agents of the Company;

C. providing at no charge, as specified from time to time by the Company, any needed personnel, equipment space and power to operate Company facilities and equipment installed on the premises of the Customer, and the level of heating and air conditioning necessary to maintain the proper operating environment on such premises;

D. obtaining, maintaining, and otherwise having full responsibility for all rights-of-way and conduits necessary for installation of fiber optic cable and associated equipment used to provide Communication Services to the Customer from the cable building entrance or property line to the location of the equipment space described in 2.3.1(C.) Any and all costs associated with obtaining and maintaining the rights-of-way described herein, including the costs of altering the structure to permit installation of the Company-provided facilities, shall be borne entirely by, or may be charged by the Company to, the Customer. The Company may require the Customer to demonstrate its compliance with this section prior to accepting an order for service;

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.3 Obligations of the Customer, (Cont'd.)

2.3.1 General, (Cont'd.)

E. providing a safe place to work and complying with all laws and regulations regarding the working conditions on the premises at which Company employees and agents shall be installing or maintaining the Company's facilities and equipment. The Customer may be required to install and maintain Company facilities and equipment within a hazardous area if, in the Company's opinion, injury or damage to the Company's employees or property might result from installation or maintenance by the Company. The Customer shall be responsible for identifying, monitoring, removing and disposing of any hazardous material (e.g. asbestos) prior to any construction or installation work;

F. complying with all laws and regulations applicable to, and obtaining all consents, approvals, licenses and permits as may be required with respect to, the location of Company facilities and equipment in any Customer premises or the rights-of-way for which Customer is responsible under Section 2.3.1D.; and granting or obtaining permission for Company agents or employees to enter the premises of the Customer at any time for the purpose of installing, inspecting, maintaining, repairing, or upon termination of service as stated herein, removing the facilities or equipment of the Company;

G. not creating, or allowing to be placed, any liens or other encumbrances on the Company's equipment or facilities; and

H. making Company facilities and equipment available periodically for maintenance purposes at a time agreeable to both the Company and the Customer. No allowance will be made for the period during which service is interrupted for such purposes.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.3 Obligations of the Customer, (Cont'd.)

2.3.2 Liability of the Customer

A. The Customer will be liable for damages to the facilities of the Company and for all incidental and consequential damages caused by the negligent or intentional acts or omissions of the Customer, its officers, employees, agents, invites, or contractors where such acts or omissions are not the direct result of the Company's negligence or intentional misconduct.

B. To the extent caused by any negligent or intentional act of the Customer as described in A., preceding, the Customer shall indemnify, defend and hold harmless the Company from and against all claims, actions, damages, liabilities, costs and expenses, including reasonable attorneys' fees, for (1) any loss, destruction or damage to property of any third party, and (2) any liability incurred by the Company to any third party pursuant to this or any other rate sheet of the Company, or otherwise, for any interruption of, interference to, or other defect in any service provided by the Company to such third party.

C. The Customer shall not assert any claim against any other Customer or user of the Company's services for damages resulting in whole or in part from or arising in connection with the furnishing of service under this rate sheet including but not limited to mistakes, omissions, interruptions, delays, errors or other defects or misrepresentations, whether or not such other Customer or user contributed in any way to the occurrence of the damages, unless such damages were caused solely by the negligent or intentional act or omission of the other Customer or user and not by any act or omission of the Company. Nothing in this rate sheet is intended either to limit or to expand Customer's right to assert any claims against third parties for damages of any nature other than those described in the preceding sentence.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.4 Customer Equipment and Channels

2.4.1 General

A User may transmit or receive information or signals via the facilities of the Company. The Company's services are designed primarily for the transmission of voice-grade telephonic signals, except as otherwise stated in this tariff. A User may transmit any form of signal that is compatible with the Company's equipment, but the Company does not guarantee that its services will be suitable for purposes other than voice-grade telephonic communication except as specifically stated in this tariff.

2.4.2 Station Equipment

A. Terminal equipment on the User's Premises and the electric power consumed by such equipment shall be provided by and maintained at the expense of the User. The User is responsible for the provision of wiring or cable to connect its terminal equipment to the Company Point of Connection.

B. The Customer is responsible for ensuring that Customer-provided equipment connected to Company equipment and facilities is compatible with such equipment and facilities. The magnitude and character of the voltages and currents impressed on Company-provided equipment and wiring by the connection, operation, or maintenance of such equipment and wiring shall be such as not to cause damage to the Company-provided equipment and wiring or injury to the Company's employees or to other persons. Any additional protective equipment required to prevent such damage or injury shall be provided by the Company at the Customer's expense, subject to prior Customer approval of the equipment expense.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.4 Customer Equipment and Channels, (Cont'd.)

2.4.3 Interconnection of Facilities

A. Any special interface equipment necessary to achieve compatibility between the facilities and equipment of the Company used for furnishing Communication Services and the channels, facilities, or equipment of others shall be provided at the Customer's expense.

B. Communication Services may be connected to the services or facilities of other communications carriers only when authorized by, and in accordance with, the terms and conditions of the tariffs of the other communications carriers that are applicable to such connections.

C. Facilities furnished under this tariff may be connected to Customer-provided terminal equipment in accordance with the provisions of this tariff. All such terminal equipment shall be registered by the Federal Communications Commission pursuant to Part 68 of Title 47, Code of Federal Regulations; and all User-provided wiring shall be installed and maintained in compliance with those regulations.

D. Users may interconnect communications facilities that are used in whole or in part for interstate communications to services provided under this tariff only to the extent that the user is an is "End User", as defined in Section 69.2(m), Title 47, Code of Federal Regulations (1992 edition).

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.4 Customer Equipment and Channels, (Cont'd.)

2.4.4 Inspections

A. Upon suitable notification to the Customer, and at a reasonable time, the Company may make such tests and inspections as may be necessary to determine that the Customer is complying with the requirements set forth in Section 2.4.2A. for the installation, operation, and maintenance of Customer-provided facilities, equipment, and wiring in the connection of Customer-provided facilities and equipment to Company-owned facilities and equipment.

B. If the protective requirements for Customer-provided equipment are not being complied with, the Company may take such action as it deems necessary to protect its facilities, equipment, and personnel. The Company will notify the Customer promptly if there is any need for further corrective action. Within ten days of receiving this notice, the Customer must take this corrective action and notify the Company of the action taken. If the Customer fails to do this, the Company may take whatever additional action is deemed necessary, including the suspension of service, to protect its facilities, equipment and personnel from harm.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.5 Payment Arrangements

2.5.1 Payment for Service

The Customer is responsible for the payment of all charges for facilities and services furnished by the Company to the Customer and to all Authorized Users by the Customer, regardless of whether those services are used by the Customer itself or are resold to or shared with other persons.

The Customer is responsible for payment of any sales, use, gross receipts, excise, access or other local, state, federal and 911 taxes, charges or surcharges (however designated) (excluding taxes on Company's net income) imposed on or based upon the provision, sale or use of Network Services.

The security of the Customer's PIN is the responsibility of the Customer. All calls placed using a PIN shall be billed to and shall be the obligation of the Customer. The Customer shall not be responsible for charges in connection with the unauthorized use of PINs arising after the Customer notifies the Company of the loss, theft, or other breach of security of such PINs.

Customers will only be charged once, on either an interstate or intrastate basis, for any nonrecurring charges.

2.5.2 Billing and Collection of Charges

The Customer is responsible for payment of all charges incurred by the Customer or other Authorized Users for services and facilities furnished to the Customer by the Company.

A. Nonrecurring charges are due and payable within thirty (30) days after the invoice date, unless otherwise agreed to in advance.

B. The Company shall present invoices for recurring charges monthly to the Customer, in advance of the month in which service is provided, and Recurring Charges shall be due and payable within thirty (30) days after the invoice date. When billing is based on customer usage, charges will be billed monthly for the preceding billing periods.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.2 Billing and Collection of Charges, (Cont'd.)

C. When service does not begin on the first day of the month, or end on the last day of the month, the charge for the fraction of the month in which service was furnished will be calculated on a pro rata basis. For this purpose, every month is considered to have thirty (30) days.

D. Billing of the Customer by the Company will begin on the Service Commencement Date, which is the first day following the date on which the Company notifies the Customer that the service or facility is available for use, except that the Service Commencement Date may be postponed by mutual agreement of the parties, or if the service or facility does not conform to standards set forth in this tariff or the Service Order. Billing accrues through and includes the day that the service, circuit, arrangement or component is discontinued.

E. If any portion of the payment is not received by the Company, or if any portion of the payment is received by the Company in funds that are not immediately available, within twenty (20) days of the mail date on the bill, then a late payment penalty shall be due the Company. The late payment penalty shall be that portion of the payment not received by the date due minus any charges billed as local taxes multiplied by 1.5%.

F. The Customer will be assessed a *maximum* charge of thirty-five ($35.00) for each check or other payment type submitted by the Customer to the Company that a bank or financial institution refuses to honor. See Section 10, Page 9 for current charges.

G. If service is disconnected by the Company in accordance with Section 2.5.6 following and later restored, restoration of service will be subject to all applicable installation charges.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.3 Disputed Bills

A. In the event that a billing dispute occurs concerning any charges billed to the Customer by the Company, the Company may require the Customer to pay the undisputed portion of the bill to avoid discontinuance of service for non-payment. The Customer must submit a documented claim for the disputed amount. The Customer will submit all documentation as may reasonably be required to support the claim. All claims must be submitted to the Company within 90 days of receipt of billing for those services. If the Customer does not submit a claim as stated above, the Customer waives all rights to filing a claim thereafter.

B. Unless disputed the invoice shall be deemed to be correct and payable in full by the Customer. If the Customer is unable to resolve any dispute with the Company, then the Customer may file a complaint with the Arizona Corporation Commission, 1200 West Washington Street, Phoenix, Arizona 85007.

C. If the dispute is resolved in favor of the Customer and the Customer has withheld the disputed amount, no interest, credits or penalties will apply.

2.5.4 Advance Payments

The Company does not collect advance payments.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.5 Deposits

A. The Company does not collect deposits.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.5 Reserved For Future Use

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SECTION 2.0 - REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.6 Discontinuance of Service

A. Upon nonpayment of any amounts owing to the Company, the Company may, by giving five (5) days written notice to the Customer, discontinue or suspend service without incurring any liability.

B. Upon violation of any of the other material terms or conditions for furnishing service the Company may, by giving five (5) days written notice to the Customer, discontinue or suspend service without incurring any liability if such violation continues during that period.

C. Upon condemnation of any material portion of the facilities used by the Company to provide service to a Customer or if a casualty renders all or any material portion of such facilities inoperable beyond feasible repair, the Company, by notice to the Customer, may discontinue or suspend service without incurring any liability.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.6 Discontinuance of Service, (Cont'd.)

D. Upon the Customer's insolvency, assignment for the benefit of creditors, filing for bankruptcy or reorganization, or failing to discharge an involuntary petition within the time permitted by law, the Company may immediately discontinue or suspend service without incurring any liability.

E. Upon any governmental prohibition or required alteration of the services to be provided or any violation of an applicable law or regulation, the Company may immediately discontinue service without incurring any liability.

F. In the event of fraudulent use of the Company's network, the Company will discontinue service without notice and/or seek legal recourse to recover all costs involved in enforcement of this provision.

G. Upon the Company's discontinuance of service to the Customer under Section 2.5.6 A. or 2.5.6 B., the Company, in addition to all other remedies that may be available to the Company at law or in equity or under any other provision of this tariff, may declare all future monthly and other charges that would have been payable by the Customer during the remainder of the term for which such services would have otherwise been provided to the Customer to be immediately due and payable (discounted to present value at six percent).

H. Without notice in the event of Customer use of equipment or services in such a manner as to adversely affect the Company's service to others.

I. Without notice in the event of tampering with the equipment or services furnished by the Company.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.7 Cancellation of Application for Service

A. Applications for service cannot be canceled without the Company's agreement. Where the Company permits a Customer to cancel an application for service prior to the start of service or prior to any special construction, no charges will be imposed except for those specified below.

B. Where, prior to cancellation by the Customer, the Company incurs any expenses in installing the service or in preparing to install the service that it otherwise would not have incurred, a charge equal to the costs incurred by the Company, less net salvage, shall apply, but in no case shall this charge exceed the sum of the charge for the minimum period of services ordered, including installation charges, and all charges others levy against the Company that would have been chargeable to the Customer had service commenced (all discounted to present value at six percent).

C. Where the Company incurs any expense in connection with special construction, or where special arrangements of facilities or equipment have begun, before the Company receives a cancellation notice, a charge equal to the costs incurred by the Company, less net salvage, applies. In such cases, the charge will be based on such elements as the cost of the equipment, facilities, and material, the cost of installation, engineering, labor, and supervision, general and administrative expense, other disbursements, depreciation, maintenance, taxes, provision for return on investment, and any other costs associated with the special construction or arrangements.

D. The special charges described in 2.5.7 A. through 2.5.7 C. will be calculated and applied on a case-by-case basis.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.5 Payment Arrangements, (Cont'd.)

2.5.8 Changes in Service Requested

If the Customer makes or requests material changes in circuit engineering, equipment specifications, service parameters, premises locations, or otherwise materially modifies any provision of the application for service, the Customer's installation fee shall be adjusted accordingly.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.6 Allowances for Interruptions in Service

Interruptions in service that are not due to the negligence of, or noncompliance with the provisions of this tariff by, the Customer or the operation or malfunction of the facilities, power or equipment provided by the Customer, will be credited to the Customer as set forth in 2.6.1 for the part of the service that the interruption affects.

2.6.1 General

A. A credit allowance will be given when service is interrupted, except as specified below. A service is interrupted when it becomes inoperative to the Customer, e.g., the Customer is unable to transmit or receive, because of a failure of a component furnished by the Company under this rate sheet.

B. An interruption period begins when the Customer reports a service, facility or circuit to be inoperative and, if necessary, releases it for testing and repair. An interruption period ends when the service, facility or circuit is operative.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.6 Allowances for Interruptions in Service, (Cont'd.)

2.6.1 General, (Cont'd.)

C. If the Customer reports a service, facility or circuit to be interrupted but declines to release it for testing and repair, or refuses access to its premises for test and repair by the Company, the service, facility or circuit is considered to be impaired but not interrupted. No credit allowances will be made for a service, facility or circuit considered by the Company to be impaired.

D. The Customer shall be responsible for the payment of service charges as set forth herein for visits by the Company's agents or employees to the premises of the Customer when the service difficulty or trouble report results from the use of equipment or facilities provided by any party other than the Company, including but not limited to the Customer.

2.6.2 Limitations of Allowances

No credit allowance will be made for any interruption in service:

A. Due to the negligence of or noncompliance with the provisions of this rate sheet by any person or entity other than the Company, including but not limited to the Customer;

B. Due to the failure of power, equipment, systems, connections or services not provided by the Company;

C. Due to circumstances or causes beyond the reasonable control of the Company;

D. During any period in which the Company is not given full and free access to its facilities and equipment for the purposes of investigating and correcting interruptions;

E. A service will not be deemed to be interrupted if a Customer continues to voluntarily make use of the such service. If the service is interrupted, the Customer can get a service credit, use another means of communications provided by the Company (pursuant to Section 2.6.3), or utilize another service provider;

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.6 Allowances for Interruptions in Service, (Cont'd.)

2.6.2 Limitations of Allowances, (Cont'd.)

F. During any period when the Customer has released service to the Company for maintenance purposes or for implementation of a Customer order for a change in service arrangements;

G. That occurs or continues due to the Customer's failure to authorize replacement of any element of special construction; and

H. That was not reported to the Company within thirty (30) days of the date that service was affected.

2.6.3 Use of Another Means of Communications

If the Customer elects to use another means of communications during the period of interruption, the Customer must pay the charges for the alternative service used.

2.6.4 Application of Credits for Interruptions in Service

A. Credits for interruptions in service that is provided and billed on a flat rate basis for a minimum period of at least one month, beginning on the date that billing becomes effective, shall in no event exceed an amount equivalent to the proportionate charge to the Customer for the period of service during which the event that gave rise to the claim for a credit occurred. A credit allowance is applied on a pro rata basis against the rates specified hereunder and is dependent upon the length of the interruption. Only those facilities on the interrupted portion of the circuit will receive a credit.

B. For calculating credit allowances, every month is considered to have thirty (30) days.

C. A credit allowance will be given for interruptions of thirty (30) minutes or more. Two or more interruptions of fifteen (15) minutes or more during any one 24-hour period shall be combined into one cumulative interruption.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.6 Allowances for Interruptions in Service, (Cont'd.)

2.6.4 Application of Credits for Interruptions in Service, (Cont'd.)

D. Interruptions of 24 Hours or Less

Length of Interruption	Amount of Service To Be Credited
Less than 30 minutes	None
30 minutes up to but not including 3 hours	1/10 Day
3 hours up to but not including 6 hours	1/5 Day
6 hours up to but not including 9 hours	2/5 Day
9 hours up to but not including 12 hours	3/5 Day
12 hours up to but not including 15 hours	4/5 Day
15 hours up to but not including 24 hours	One Day

E. Interruptions Over 24 Hours and Less Than 72 Hours

Interruptions over 24 hours and less than 72 hours will be credited 1/5 day for each 3-hour period or fraction thereof. No more than one full day's credit will be allowed for any period of 24 hours.

F. Interruptions Over 72 Hours

Interruptions over 72 hours will be credited 2 days for each full 24-hour period. No more than thirty (30) days credit will be allowed for any one month period.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.6 Allowances for Interruptions in Service, (Cont'd.)

2.6.5 Cancellation For Service Interruption

Cancellation or termination for service interruption is permitted only if any circuit experiences a single continuous outage of 8 hours or more or cumulative service credits equaling 16 hours in a continuous 12-month period. The right to cancel service under this provision applies only to the single circuit that has been subject to the outage or cumulative service credits.

2.7 Use of Customer's Service by Others

2.7.1 Joint Use Arrangements

Joint use arrangements will be permitted for all services provided under this tariff. From each joint use arrangement, one member will be designated as the Customer responsible for the manner in which the joint use of the service will be allocated. The Company will accept orders to start, rearrange, relocate, or discontinue service only from the designated Customer. Without affecting the Customer's ultimate responsibility for payment of all charges for the service, each joint user shall be responsible for the payment of the charges billed to it.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.8 Cancellation of Service/Termination Liability

If a Customer cancels a Service Order or terminates services before the completion of the term for any reason whatsoever other than a service interruption (as defined in Section 2.6.1 above), the Customer agrees to pay to the Company termination liability charges, as defined below. These charges shall become due as of the effective date of the cancellation or termination and be payable within the period, set forth in Section 2.5.2.

2.8.1 Termination Liability

The Customer's termination liability for cancellation of service shall be equal to:

A. all unpaid Non-Recurring charges reasonably expended by the Company to establish service to the Customer; plus

B. any disconnection, early cancellation or termination charges reasonably incurred and paid to third parties by the Company on behalf of the Customer; plus

C. all Recurring Charges specified in the applicable Service Order Tariff for the balance of the then current term discounted at the prime rate announced in the Wall Street Journal on the third business day following the date of cancellation;

D. minus a reasonable allowance for costs avoided by the Company as a direct result of the Customer's cancellation.

2.9 Transfers and Assignments

Neither the Company nor the Customer may assign or transfer its rights or duties in connection with the services and facilities provided by the Company without the written consent of the other party, except that the Company may assign its rights and duties:

2.9.1 to any subsidiary, parent company or affiliate of the Company; or

2.9.2 pursuant to any sale or transfer of substantially all the assets of the Company; or

2.9.3 pursuant to any financing, merger or reorganization of the Company.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.10 Customer Liability for Unauthorized Use of the Network

Unauthorized use of the network occurs when a person or entity that does not have actual, apparent, or implied authority to use the network, obtains the Company's services provided under this rate sheet.

2.10.1 Customer Liability for Fraud and Unauthorized Use of the Network

A. The Customer is liable for the unauthorized use of the network obtained through the fraudulent use of a Company calling card, if such a card is offered by the Company, or an accepted credit card, provided that the unauthorized use occurs before the Company has been notified.

B. A Company calling card is a telephone calling card issued by the Company at the Customer's request, which enables the Customer or user(s) authorized by the Customer to place calls over the Network and to have the charges for such calls billed to the Customer's account.

An accepted credit card is any credit card that a cardholder has requested or applied for and received, or has signed, used, or authorized another person to use to obtain credit. Any credit card issued as an renewal or substitute in accordance with this paragraph is an accepted credit card when received by the cardholder.

C. The Customer must give the Company written or oral notice that an unauthorized use of a Company calling card or an accepted credit card has occurred or may occur as a result of loss, and/or theft.

D. The Customer is responsible for payment of all charges for calling card services furnished to the Customer or to users authorized by the Customer to use service provided under this rate sheet, unless due to the negligence of the Company. This responsibility is not changed due to any use, misuse, or abuse of the Customer's service or Customer-provided equipment by third parties, the Customer's employees, or the public.

The liability of the Customer for unauthorized use of the Network by credit card fraud will not exceed the lesser of fifty dollars ($50.00) or the amount of money, property, labor, or services obtained by the unauthorized user before notification to the Company.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.11 Notices and Communications

2.11.1 The Customer shall designate on the Service Order an address to which the Company shall mail or deliver all notices and other communications, except that the Customer may also designate a separate address to which the Company's bills for service shall be mailed.

2.11.2 The Company shall designate on the Service Order an address to which the Customer shall mail or deliver all notices and other communications, except that Company may designate a separate address on each bill for service to which the Customer shall mail payment on that bill.

2.11.3 Except as otherwise stated in this tariff, all notices or other communications required to be given pursuant to this tariff will be in writing. Notices and other communications of either party, and all bills mailed by the Company, shall be presumed to have been delivered to the other party on the third business day following placement of the notice, communication or bill with the U.S. Mail or a private delivery service, prepaid and properly addressed, or when actually received or refused by the addressee, whichever occurs first.

2.11.4 The Company or the Customer shall advise the other party of any changes to the addresses designated for notices, other communications or billing, by following the procedures for giving notice set forth herein.

2.12 Taxes, Fees and Surcharges

The Company reserves the right to bill any and all applicable taxes, fees and surcharges in addition to normal rates and charges for services provided to the Customer. Taxes and fees include, but are not limited to: Federal Excise Tax, State Sales Tax, Municipal Tax, and Gross Receipts Tax. Unless otherwise specified in this tariff, such taxes, fees and surcharges are in addition to rates as quoted in this tariff and will be itemized separately on Customer invoices.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.12 Taxes, Fees and Surcharges, (Cont'd.)

2.12.1 Arizona Universal Service Fund (AUSF)

In addition to all other taxes and fees that are listed herein or passed through in the normal course of business (e.g. sales tax), the Company shall also add an amount to be collected to each bill for recovery of the Arizona Universal Service Fund (AUSF).

Towards the ultimate goal that basic service be available and affordable to all citizens of the state, the Arizona Corporation Commission has created support mechanisms to assist in the provision of such service in high-cost areas. Pursuant to Arizona Administrative Code, R14-2, Article 12, the Rule directs that the surcharge will be levied on all telecommunications service purchased by end-users.

The Arizona Universal Service Fund (AUSF) surcharge will be the amount set forth in the Arizona Administrative Code, R14-2, Article 12. The percentage and amounts set forth will be subject to periodic adjustment by the Company.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.13 Miscellaneous Provisions

2.13.1 Telephone Number Changes

Whenever any Customer's telephone number is changed after a directory is published, the Company shall intercept all calls to the former number for at least one hundred and twenty (120) days and give the calling party the new number provided existing central office equipment will permit, and the Customer so desires.

When service in an existing location is continued for a new Customer, the existing telephone number may be retained by the new Customer only if the former Customer consents in writing, and if all charges against the account are paid or assumed by the new Customer.

2.13.2 Maintenance and Operations Records

Records of various tests and inspections, to include non-routine corrective maintenance actions or monthly traffic analysis summaries for network administration, necessary for the purposes of the Company or to fulfill the requirements of Commission rules shall be kept on file in the office of the Company as required under Commission rules.

SECTION 2.0 - REGULATIONS, (CONT'D.)

2.14 Customer Responsibility

A. Cancellation by Customer

Customers may cancel service verbally or in writing. The company shall hold the Customer responsible for payment of all charges, including fixed fees, surcharges, etc., which accrue up to the cancellation date. Customers that cancel the primary local exchange line will have the entire Account disconnected, including any secondary line and all associated features. In the event the Customer executes a term commitment agreement with the Company, the Customer must cancel service and terminate the agreement in accordance with the agreement terms.

SECTION 3.0 - SERVICE AREAS

3.1 Exchange Service Areas

Local exchange services are provided, subject to availability of facilities and equipment, in areas currently served by the following Incumbent LECs: 1) Qwest, Inc.

SECTION 4.0 - BASIC SERVICES AND RATES

4.1 Call Timing for Usage Sensitive Services

Where charges for a service are specified based on the duration of use, such as the duration of a telephone call, the following rules apply:

4.1.1 Calls are measured in durational increments identified for each service. All calls which are fractions of a measurement increment are rounded-up to the next whole unit.

4.1.2 Timing on completed calls begins when the call is answered by the called party. Answering is determined by hardware answer supervision in all cases where this signaling is provided by the terminating local carrier and any intermediate carrier(s).

4.1.3 Timing terminates on all calls when the calling party hangs up or the Company's network receives an off-hook signal from the terminating carrier.

4.2 Reserved for Future Use

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service

4.3.1 General

Inter-Tel offers basic local exchange service only as part of a bundle or package of telecommunications services. All packages include local service, long distance service (interstate and intrastate toll) and selected custom calling features. Voice Mail and Optional Internet access 1 may be available with some packages at an additional charge. The aforementioned services are only available as part of the bundled service offering and are not available on an individual service basis. Customers will be billed directly by the Company.

The Company provides Customers with the option of obtaining a Primary Line and Secondary Line per account:

A. Primary Line

The initial residential local exchange access line per account.

B. Secondary Line

The second or additional residential local exchange access line, billed to the same address as the Primary Line, the Secondary Line will share the monthly call allowance with the Primary Line. The Secondary Line does not automatically include or share any Custom Calling Features. Feature packages may be purchased separately.

Should a Customer with both lines opt to disconnect the Primary Line, the remaining Secondary Line will automatically convert to a Primary Line with all features and functionality of such, and at the Primary Line monthly recurring rate.

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SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.1 General, (Cont'd.)

Network Exchange Bundled Service may include the calling features listed below:

These features are offered subject to availability of suitable facilities. Certain features may not be available with all classes of services.

Call Forwarding - Fixed, Busy Line No Answer - This feature, when activated, redirects attempted terminating calls to another Customer-specified line. Call originating ability is not affected by Call Forwarding - Fixed, Busy Line No Answer. The calling party is billed for the call to the called number. If the forwarded leg of the call is chargeable, the Customer with the Call Forwarding - Fixed, Busy Line No Answer is billed for the forwarded leg of the call. Calls cannot be transferred to an International Direct Distance Dialing number.

Caller ID with Name - Allows a Customer to see a caller's name and number previewed on a display screen before the call is answered allowing a Customer to prioritize and or screen incoming calls. Caller ID records the name, number, date and time of each incoming call - including calls that aren't answered by the Customer. Caller ID service requires the use of specialized CPE not provided by the company. It is the responsibility of the Customer to provide the necessary CPE. In areas where Caller ID with Name is not available, Caller ID, which only displays the incoming telephone number, will be substituted.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.1 General, (Cont'd.)

Network Exchange Bundled Service may include the calling features listed below, (cont'd.):

Call Forwarding - Variable - a Customer activated feature that automatically transfers all incoming calls from the Customer's telephone number to another dialable telephone number until the Customer deactivates the feature. If forwarded to a long distance number the Subscriber will incur the long distance charges.

Call Forwarding with Remote Activation- This service allows Customers who subscribe to Call Forward to access, activate, or deactivate Call Forward from a remote location using a touchtone telephone. If forwarded to a long distance number the Subscriber will incur the long distance charges.

Call Trace - Allows a called party to initiate an automatic trace of the last call received. Call Trace is available on a usage basis only. After receiving the call which is to be traced, the Customer dials a code and the traced telephone number is automatically sent to the Company for action. The Customer originating the trace will not receive the traced telephone number. The results of the trace will be furnished only to legally constituted law enforcement agencies or authorities upon proper request by them.

Call Blocking- Call Blocking allows Customer to block calls from different telephone numbers. A screening list is created by Customer either by adding the last number associated with the line (incoming or outgoing) or by pre-selecting the telephone number to be blocked. Callers from such numbers hear an announcement that the calling party is not accepting calls and Customer's phone will not ring. The screening list may be edited and revised at Customer's discretion.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.1 General, (Cont'd.)

Network Exchange Bundled Service may include the calling features listed below, (cont'd.):

Caller ID Per Line Blocking- Allows a Customer to prevent the transmission and display of their directory number and/or directory name information on outgoing calls. Line Blocking is in operation on a continuous basis and is applicable on all outgoing calls from Customer's blocked line. Line Blocking does not prevent transmission of the calling party information to emergency services that utilize automatic number identification for delivery of the calling information.

VIP Alert - Allows a customer to program telephone numbers of selected callers, enabling the customer to distinguish certain incoming calls from all others by a distinctive ring tone.

Privacy Service- A feature which intercepts calls that are marked "private" and "out of area," or "unavailable" on Caller ID units. When unidentified callers dial the Subscribers number, they will receive an announcement informing them that the party they are calling does not accept calls from unidentified callers. They will receive a prompt to identify their name or state their intention and the service will then attempt to connect the call. Only if the caller responds will the call be connected.

The Subscriber's Caller ID will display the platform number and the name of the service. If the Subscriber chooses not to take the call the caller will hear a message which states the Subscriber is unavailable.

Privacy Service is offered subject to availability of suitable facilities. This service will be provisioned on a line-by-line basis and Customers with more than one line would need to have the service activated on each line if they want the ability to intercept unknown and blocked calls to each line.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.1 General, (Cont'd.)

Call Waiting with Caller ID with Name - Call Waiting with Caller ID with Name provides a tone signal to indicate to a Customer already engaged in a telephone call that a second caller is attempting to dial in and allows a Customer to see a caller's name and number previewed on a display screen allowing a Customer to prioritize and or screen incoming calls. This feature permits the Customer to place the first call on hold, answer the second call and then alternate between both callers. Cancel Call Waiting (CCW) allows a Call Waiting (CW) Customer to disable CW for the duration of an outgoing telephone call. CCW is activated (i.e., CW is disabled) by dialing a special code prior to placing a call, and is automatically deactivated when the Customer disconnects from the call. In areas where Caller ID with Name is not available, Caller ID, which only displays the callers telephone number, will be substituted.

Speed Calling - This feature allows a user to dial selected numbers by means of an abbreviated code. This feature is available in either an 8 number or a 30 number capacity. The Speed Calling list can only accommodate a number consisting of 15 digits or less.

Three Way Calling - Permits the Customer to add a third party to an established connection. When the third party answers, a two-way conversation can be held before adding the original party for a three-way conference. The Customer initiating the conference controls the call and may disconnect the third party to reestablish the original connection or establish a connection to a different third party. The feature may be used on both outgoing and incoming.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.2 Arizona Home Edition - Standard Service

Arizona Home Edition is a package of features available to residential customers in conjunction with an individual flat rate or additional flat rate access line. Residence customers are entitled to choose three services/features from the following list in their package.

- Anonymous Call Rejection
- Caller ID – Name and Number
- Call Forwarding Busy Line/Don't Answer
- Call Following
- Call Forwarding Variable
- Selective Call Forwarding
- Call Rejection
- Call Waiting
- Call Waiting ID
- Selective Call Waiting
- Custom Ringing (first Custom Ringing number only)
- Directory Assistance (6 calls above allowance)
- Last Call Return
- Message Waiting Indication – Audible or Audible/Visual
- Three-Way Calling

All terms and conditions specified elsewhere for the respective services/features requested as part of this package shall apply.

a. A customer may choose one or more of the features in the Caller ID Family as one of their selections

b. A customer may choose Call Waiting, Call Waiting ID or Selective Call Waiting from the Call Waiting Family as one of their selections.

c. A customer choosing Caller ID - Name and Number will automatically be provided with Anonymous Call Rejection.

d. All services or features selected in the package can only be provided where technically available and compatible with other features the customer may choose to order.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.2 Arizona Home Edition - Standard Service, (Cont'd.)

Rates

Arizona Home Edition will be provided at the following rates:

	MAXIMUM MONTHLY RATE
• Per individual flat rate residence line with three features	$25.00
• Per additional flat rate residence line with three features	30.00

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.3 Arizona Home Edition - Deluxe Service

Arizona Home – Deluxe Edition is a package of features available to residential customers in conjunction with an individual flat rate or additional flat rate access line. Residence customers subscribing to the package are entitled to unlimited use of the services/features specified below:

- Anonymous Call Rejection
- Caller ID – Name and Number
- Call Forwarding Busy Line/Don't Answer
- Call Following
- Call Forwarding Variable
- Selective Call Forwarding
- Call Rejection
- Call Waiting
- Call Waiting ID
- Selective Call Waiting
- Custom Ringing (first Custom Ringing number only)
- Directory Assistance (6 calls above allowance)
- Last Call Return
- Message Waiting Indication – Audible or Audible/Visual
- Three-Way Calling

All terms and conditions specified elsewhere for the respective services/features requested as part of this package shall apply.

a. A customer may choose one or more of the features in the Caller ID Family as one of their selections

b. A customer may choose Call Waiting, Call Waiting ID or Selective Call Waiting from the Call Waiting Family as one of their selections.

c. A customer choosing Caller ID - Name and Number will automatically be provided with Anonymous Call Rejection.

d. All services or features selected in the package can only be provided where technically available and compatible with other features the customer may choose to order.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.3 Arizona Home Edition - Deluxe Service, (Cont'd.)

Rates

Arizona Home Edition – Deluxe Service will be provided at the following rates:

	MAXIMUM MONTHLY RATE
• Per individual flat rate residence line with three features	$40.00
• Per additional flat rate residence line with three features	40.00

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SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.3 RESERVED FOR FUTURE USE

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.4 Arizona Home Edition - Deluxe Service

Package Price for Deluxe Service

	Maximum
Primary Line, per month	$130.00
Secondary Line, per month	$100.00
Service Connection Fee, one time charge per line *	
Primary Line	$130.00
Secondary Line	$100.00

* Service Connection fee waived for those customers who meet the Company's enrollment criteria and who retain their existing telephone number when switching their service to Inter-Tel.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

RESERVEED FOR FUTURE USE

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SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.5 Business A La Carte Service

Business A La Carte service is targeted at small business Customers and provides options based on the Customers calling patterns and estimated usage. . Customers who subscribe to this service must designate Inter-Tel as the presubscribed carrier for local calling concurrent with enrollment for this service. Business A La Carte provides Customers with the option of selecting Inter-Tel for toll services.

A. Local Exchange Service

.1 Local Access Line

	Maximum
Local Business Line	
Monthly Rate	$120.00
Service Connection Fee, one-time charge per line [1]	
Per Line	$200.00

.2 PBX

	Maximum
Monthly Rate	$120.00
Service Connection Fee, one-time charge per line [1]	
Per Line	$200.00

1 Service Connection fee is waived for those customers who retain their existing telephone number when switching their service to Inter-Tel. The charge will apply if additional lines are transferred to Inter-Tel after the initial order.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.5 Business A La Carte Service, (Cont'd.)

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SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.5 Business A La Carte Service, (Cont'd.)

RESERVED FOR FUTURE USE

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.5 Business A La Carte Service, (Cont'd.)

RESERVED FOR FUTURE USE

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.5 Business A La Carte Service, (Cont'd.)

E. Custom/Optional Calling Features

Business A La Carte may include the calling features listed below:

Call Forwarding - Call Forwarding, when activated, redirects attempted terminating calls to another Customer-specific line. The Customer may have to activate and deactivate the forwarding function and specify the desired terminating telephone number during each activation procedure. Call originating ability is not affected by Call Forwarding. The calling party is billed for the call to the called number. If the forwarded leg of the call is chargeable, the Customer with the Call Forwarding is billed for the forwarded leg of the call. Calls cannot be transferred to an International Direct Distance Dialing number.

Speed Calling - This feature allows a user to dial selected numbers by means of an abbreviated code. This feature is available in an 8 number capacity. The Speed Calling list can only accommodate a number consisting of 15 digits or less.

Caller ID - Allows a Customer to see a caller's telephone number previewed on a display screen before the call is answered allowing a Customer to prioritize and or screen incoming calls. Caller ID records the number, date and time of each incoming call - including calls that aren't answered by the Customer. Caller ID service requires the use of specialized CPE not provided by the company. It is the responsibility of the Customer to provide the necessary CPE.

Call Waiting - Call Waiting provides a tone signal to indicate to a Customer already engaged in a telephone call that a second caller is attempting to dial in. This feature permits the Customer to place the first call on hold, answer the second call and then alternate between both callers. Cancel Call Waiting (CCW) allows a Call Waiting (CW) Customer to disable CW for the duration of an outgoing telephone call. CCW is activated (i.e., CW is disabled) by dialing a special code prior to placing a call, and is automatically deactivated when the Customer disconnects from the call. Customers must actively choose this feature on a line-by-line basis. Call Waiting is not available on lines enabled for Rotary Hunting.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.5 Business A La Carte Service, (Cont'd.)

E. Custom/Optional Calling Features, (Cont'd.)

Three Way Calling - Permits the Customer to add a third party to an established connection. When the third party answers, a two-way conversation can be held before adding the original party for a three-way conference. The Customer initiating the conference controls the call and may disconnect the third party to reestablish the original connection or establish a connection to a different third party. The feature may be used on both outgoing and incoming.

Hunting - Routes a call to an idle station line in a prearranged group when the called station line is busy. This feature is available at no charge but must be requested by the Customer.

a. Maximum rates

.1	Monthly Rates, per Feature:	$15.00
.2	Monthly Rate, Feature Pack, (3 or more features):	$45.00

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.6 Arizona Business Edition - Standard Service

Business Edition - Standard is a package of features available to business customers in conjunction with an individual flat rate or additional flat rate access line. Business customers subscribing to the package are entitled to choose three services/features from the following list in their package.

- Anonymous Call Rejection
- Caller ID - Name and Number
- Call Forwarding Busy Line
- Call Forwarding Busy Line/Don't Answer
- Call Forwarding Don't Answer
- Call Forwarding Variable
- Remote Access Forwarding
- Call Transfer
- Call Waiting
- Call Waiting ID
- Selective Call Waiting
- Custom Ringing
- Directory Assistance (6 calls above allowance)
- Last Call Return
- Message Waiting Indication – Audible or Audible/Visual
- Three-Way Calling

Terms and Conditions

a. All terms and conditions specified elsewhere for the respective services/features requested as part of this package shall apply.

b. A customer choosing Caller ID - Name and Number will automatically be provided with Anonymous Call Rejection.

c. A customer may choose one or more compatible features in the Call Forwarding Family as one of their selections.

d. A customer may choose Call Waiting, Call Waiting ID or Selective Call Waiting from the Call Waiting Family as one of their selections. They may add Long Distance Alert as part of that selection.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.6 Arizona Business Edition - Standard Service, (Cont'd.)

Terms and Conditions, (Cont'd.)

e. A customer who chooses Voice Messaging Service will also be provided with Call Forwarding Busy Line/Don't Answer, Easy Access and Message Waiting Indication as part of their Voice Messaging Service selection. A customer who wishes to use another provider's Voice Messaging Service will be provided with Call Forwarding Busy Line/Don't Answer, Easy Access and Message Waiting Indication and it will not be counted as one of their three selections of features/services.

f. All services or features selected in the package can only be provided where technically available and compatible with other features the customer may choose to order.

g. Customers selecting Directory Assistance may make six calls above the allowance to the Company's 411 service.

Rates and Charges

a. The monthly rate that follows includes a business individual flat rate or additional flat rate line as specified in 4.3.5A, preceding. Where applicable, incremental charges, apply.

b. Normal nonrecurring charges associated with the line as specified in 4.3.5, preceding, apply where the Company's Business is provided in association with the installation of a new business individual or additional flat rate line or the move of a business individual or additional flat rate line from one location to another.

c. Any mandated charges or special surcharges, e.g., 911, TDD, EUCL, Telephone Assistance Plan, will apply to Add-A-Line under the same terms as a flat rate business line.

d. Arizona Business Edition - Standard Service will be provided at the following rate:

	MAXIMUM MONTHLY RATE
Per individual or additional flat rate business line	$75.00

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.7 Arizona Business Edition - Deluxe Service

Business Edition - Deluxe is a package of features available to business customers in conjunction with an individual flat rate or additional flat rate access line. Business customers subscribing to the package are entitled to unlimited use of the services/features specified below:

- Anonymous Call Rejection
- Caller ID - Name and Number
- Call Forwarding Busy Line
- Call Forwarding Busy Line/Don't Answer
- Call Forwarding Don't Answer
- Call Forwarding Variable
- Remote Access Forwarding
- Call Transfer
- Call Waiting
- Call Waiting ID
- Selective Call Waiting
- Custom Ringing
- Directory Assistance (6 calls above allowance)
- Last Call Return
- Message Waiting Indication – Audible or Audible/Visual
- Three-Way Calling

Terms and Conditions

a. All terms and conditions specified elsewhere for the respective services/features requested as part of this package shall apply.

b. A customer choosing Caller ID - Name and Number will automatically be provided with Anonymous Call Rejection.

c. A customer may choose one or more compatible features in the Call Forwarding Family as one of their selections.

SECTION 4.0 - BASIC SERVICES AND RATES, (CONT'D.)

4.3 Network Exchange Bundled Service, (Cont'd.)

4.3.7 Arizona Business Edition - Deluxe Service, (Cont'd)

Terms and Conditions, (Cont'd.)

d. A customer may choose Call Waiting, Call Waiting ID or Selective Call Waiting from the Call Waiting Family as one of their selections. They may add Long Distance Alert as part of that selection.

e. A customer who chooses Voice Messaging Service will also be provided with Call Forwarding Busy Line/Don't Answer, Easy Access and Message Waiting Indication as part of their Voice Messaging Service selection. A customer who wishes to use another provider's Voice Messaging Service will be provided with Call Forwarding Busy Line/Don't Answer, Easy Access and Message Waiting Indication and it will not be counted as one of their three selections of features/services.

f. All services or features selected in the package can only be provided where technically available and compatible with other features the customer may choose to order.

g. Customers selecting Directory Assistance may make six calls above the allowance to the Company's 411 service.

Rates and Charges

a. The monthly rate that follows includes a business individual flat rate or additional flat rate line as specified in 4.3.5A, preceding. Where applicable, incremental charges, apply.

b. Normal nonrecurring charges associated with the line as specified in 4.3.5, preceding, apply where the Company's Business is provided in association with the installation of a new business individual or additional flat rate line or the move of a business individual or additional flat rate line from one location to another.

c. Any mandated charges or special surcharges, e.g., 911, TDD, EUCL, Telephone Assistance Plan, will apply to Add-A-Line under the same terms as a flat rate business line.

d. Arizona Business Edition - Deluxe will be provided at the following rate:

	MAXIMUM MONTHLY RATE
Per individual or additional flat rate business line	$100.00

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES

5.1 Service Order and Change Charges

Non-recurring charges apply to processing Service Orders for new service and for changes in service.

5.1.1 Service Order Charges

	Maximum Rates	
	Residence	**Business**
Primary and Secondary Service Connection Charge	$50.00	$80.00
Transfer of Service Charge, Primary Line	$110.00	$130.00
Transfer of Service Charge, Secondary Line	$110.00	$130.00
Technician Dispatch Charge (or Trouble Isolation Charge)	$160.00	$160.00
Service Order Charge	$30.00	$30.00
Premises Visit Charge, first 15 minutes	80.00	80.00
Premises Visit Charge, add'l 15 minutes	60.00	60.00

5.1.2 Change Order Charges:

Telephone Number Change Order	$20.00	$55.00
Feature or Feature Pack Change Order	$20.00	$55.00
Toll Restriction Fee Order	$20.00	$55.00
Listing Change Charge	$20.00	$55.00
Home Edition Change Charge	$20.00	$55.00

5.1.3 Record Change Charges

Record Order Charge	15.00	45.00

5.1.4 Miscellaneous Charges

Duplicate Invoice	$25.00	$25.00
Call Detail Report	$25.00	$25.00

Service Connection Fees are listed with the rates for the specific service tariffed.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.1 Service Order and Change Charges, (Cont'd.)

5.1.5 Service Order Charges – Definitions

Primary Service Connection Charge - applies to requests for initial connection or establishment of telephone service to the Company.

Secondary Service Connection Charge - applies to the second or additional line of a new access line installation and connection and customer requests for an inside move, change or addition to regular service. This charge applies only when the second or additional line is ordered simultaneously with the initial connection for service.

Transfer of Service Charge, Primary Line - applies to the first line of a Transfer of Service Order, (TOS) when a customer requests a move or change in physical location. This charge applies whether a customer changes telephone number or not. If, in addition, the Customer requests the telephone number be changed, a separate charge may apply.

Transfer of Service Charge, Secondary Line - applies to the second, or third, etc., line of a Transfer of Service Order, (TOS) when a customer requests a move or change in physical location. This charge applies whether a customer changes telephone number or not. If, in addition, the Customer requests the telephone number be changed, a separate charge may apply.

Technician Dispatch (or Trouble Isolation) Charge - A separate Technician Dispatch Charge (or Trouble Isolation Charge) applies, in addition to all other charges for the visit, when a visit to the Customer's premises is necessary to isolate a problem reported to the Company but identified by the Company's technician as attributable to Customer-provided equipment or inside wire. This charge also applies for visits by the Company's agents or employees, at the Customer's request, to the Premises of the Customer, when the Customer fails to meet the Company's agent or employees for the prearranged appointment as requested.

Service Order Charge - This charge, applicable to Business Customers only, applies to customer-requested changes in service not covered specifically on other identified non-recurring service order and change charges. This charge is applied in cases where Hunting is added after the initial order is placed.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.1 Service Order and Change Charges, (Cont'd.)

5.1.6 Change Order Charges – Definitions

Change Order Charges apply to work associated with providing exchange line service or customer-requested changes to existing services. One charge applies for each change order requested by the customer. If multiple changes listed below are requested by the Customer and occur on the same order/request one charge only applies. A Change Order Service Charge applies to the following customer-initiated changes:

Feature or Feature Pack Change Order - applies when a customer requests a change, adding or removing a feature or feature pack.

Toll Restriction Fee Order - applies when a Customer requests a change, adding or removing Toll Restriction Service.

Telephone Number Change Order - applies to each telephone number change request/order.

Long Distance Minutes Pack Change Order - applies to residential Customers who request/order a change to add or delete an LD Minutes Pack.

Listing Change Charge - applies when a Customer requests/orders a change to add or delete a white pages listing or requests a change to add/delete listings. This charge also applies to request for Non-Published or Non-Listed numbers.

Home Edition Change Charge - applies when a residential Customer requests/orders a change in service from Home Edition- Basic Service to Home Edition- Standard Service or from Home Edition - Standard Service to Home Edition - Basic Service.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.1 Service Order and Change Charges, (Cont'd.)

5.1.7 Record Change Charges – Definitions

A Record Change charge applies when a Customer requests/orders a change to Company records such as adding/changing a name on said Customer's account, changing billing address or contact information, adding/changing the person(s) authorized to make changes on said Customer's account.

5.1.8 Miscellaneous Charges – Definitions

Duplicate Invoice - applies each time a Customer requests an additional copy of a current bill or invoice.

Call Detail Report - applies each time a Customer requests local call detail for a given month.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.2 Reserved For Future Use

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.2 Reserved For Future Use

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.3 Restoration of Service

A restoration charge applies to the restoration of suspended service and facilities because of nonpayment of bills and is payable at the time that the restoration of the suspended service and facilities is arranged. The restoration charge does not apply when, after disconnection of service, service is later re-installed.

	Maximum Rates	
	Residence	**Business**
Per occasion, per line	$50.00	$110.00

5.4 Temporary Suspension/Restoration of Service

Upon the request of the customer, service may be temporarily suspended. Suspension of service may begin or terminate on any day of the month provided notice is given sufficiently in advance for arrangements to be made. Service will be disconnected to the extent necessary to assure than no inward or outward service will be available during the period of suspension.

	Maximum Rates	
	Residence	**Business**
Nonrecurring charge, per line suspended	$20.00	$55.00
Recurring charge, per line suspended	50% of regular service rates	
Nonrecurring charge, per line restored	$20.00	$55.00

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.5 Public Telephone Surcharge

In order to recover the Company's expenses to comply with the FCC's pay telephone compensation plan effective on October 7, 1997 (FCC 97-371), an undiscountable per call charge is applicable to all intrastate calls that originate from any pay telephone, not presubscribed to the Company, used to access Company provided services. This surcharge, which is in addition to standard tariffed usage charges and any applicable service charges and surcharges associated with service, applies for the use of the instrument used to access Company provided service and is unrelated to the service accessed from the pay telephone.

Pay telephones include coin-operated and coinless phones owned by local telephone companies, independent companies and interexchange carriers. The Public Pay Telephone Surcharge applies to the initial completed call and any reoriginated call. The Public Pay Telephone Surcharge does not apply to calls placed from pay telephones at which the Customer pays for service by inserting coins during the progress of the call.

Whenever possible, the Public Pay Telephone Surcharge will appear on the same invoice containing the usage charges for the surcharged call. In cases where proper pay telephone coding digits are not transmitted to the Company prior to completion of a call, the Public Pay Telephone Surcharge may be billed on a subsequent invoice after the Company has obtained information from a carrier that the originating station is an eligible pay telephone.

Maximum Rate Per Call: $1.00

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SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.6 Optional Calling Features

The features in this section are made available to Residential and Business Customers on a per use basis. All features are provided subject to availability. Customers may utilize each feature by dialing the appropriate access code. The Customer will be billed the per feature activation charge shown in the table below each time a feature is used by the Customer. Transmission levels for calls forwarded or calls placed or received using optional calling features may not be acceptable for all some uses in some cases.

5.6.1 Feature Descriptions

Return Call: Allows a Customer to return the most recent incoming call and, after dialing a code, hear an announcement of the last telephone number that called. If the Customer wishes to return the call right away, voice prompts will instruct the Customer to dial a certain digit and the call will automatically be returned.

Call Trace: Allows a Customer to initiate an automatic trace of the last call received. After receiving the call which is to be traced, the Customer dials a code and the traced telephone number is automatically sent to the Company. The Customer using Call Trace is required to contact the Company for further action. The Customer originating the trace will not receive the traced telephone number. The results of a trace will be furnished only to legally constituted authorities upon proper request by them.

Repeat Dialing: Permits the Customer to redial automatically the last number dialed.

Three Way Calling: permits the Customer to add a third party to an established connection. When the third party answers, a two-way conversation can be held before adding the original party for a three-way conference. The Customer initiating the conference controls the call and may disconnect the third party to reestablish the original connection or establish a connection to a different third party. The feature may be used on both outgoing and incoming.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.6 Optional Calling Features, (Cont'd.)

5.6.1 Feature Descriptions, (Cont'd.)

Caller Identification Blocking: Allows the name and number of the calling party to be blocked from being transmitted when placing outbound calls.

Per Call Blocking: To activate per-call blocking, a Customer dials a special code prior to placing a call. Blocking will be activated for that outgoing call only. There is no charge for using per call blocking, and it is provided on an unlimited basis.

Per Line Blocking: When blocking is established on the line, it can be deactivated by dialing a code before each call. This one call unblock allows the name and/or number to be sent for that one call only. Customers who choose per line blocking for the first time will not be charged the nonrecurring charge. After the first time, customers requesting per line blocking will pay a nonrecurring charge for each line equipped with per line blocking. Per line blocking will be provided free to law enforcement and domestic violence agencies and individual victims of domestic violence upon request.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.6 Optional Calling Features, (Cont'd.)

5.6.2 Maximum Rates

FEATURE	Residential Monthly Maximum	Business Monthly Maximum
Speed Calling		
8 Number	12.00	12.00
30 Number	12.00	12.00
Call Forwarding		
Variable	12.00	12.00
Busy Line (Expanded)	12.00	12.00
Busy Line (Overflow)	12.00	12.00
Busy Line (Programmable)	12.00	12.00
Don't Answer	12.00	12.00
Don't Answer (Expanded)	12.00	12.00
Don't Answer (Programmable)	12.00	12.00
Busy Line/Don't Answer	12.00	12.00
Busy Line (External)/DA	12.00	12.00
Call Rejection	12.00	12.00
Call Waiting	12.00	12.00
Call Transfer	12.00	12.00
Caller ID		
Name and Number	12.00	12.00
Number	12.00	12.00
Continuous Redial	12.00	12.00
Distinctive Alert	12.00	12.00
Hot Line	12.00	12.00
Priority Call	12.00	12.00
Remote Access Forwarding	12.00	12.00
Selective Call Forwarding	12.00	12.00

FEATURE	Residential Per Use	Residential Monthly Maximum	Business Per Use	Business Monthly Maximum
Call Tracing - per use	$4.00	$12.00	$4.00	$12.00
Repeat Call (*66) - per use	$1.50	$12.00	$1.50	$12.00
Return Call (*69) - per use	$1.50	$12.00	$1.50	$12.00
Three Way Calling - per use	$1.50	$12.00	$1.50	$12.00

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.7 Directory Assistance Services

A Customer may obtain assistance, for a charge, in determining a telephone number by dialing Directory Assistance Service. A Customer can also receive assistance by writing the Company with a list of names and addresses for which telephone numbers are desired.

5.7.1 Basic Directory Assistance

The rates specified following apply when Customers request company assistance in determining telephone numbers of Customers who are located in the same local service area or who are not located in the same local service area but who are located within the same NPA.

There are no call allowances for Directory Assistance.

Charges will not apply for calls placed from hospital services or calls placed from telephones where the Customer or, in the case of residence service, a member of the Customer's household, has been affirmed in writing as unable to use a Company provided directory because of a visual, physical or reading handicap.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.7 Directory Assistance Services, (Cont'd.)

5.7.2 Directory Assistance Call Completion

Directory Assistance Call Completion (DACC) is a service that provides customers the option of having their local or intraLATA calls automatically completed when they request a telephone listing from the Directory Assistance operator. The call may be completed automatically or by the Directory Assistance operator.

The DACC portion of the call may either be billed in the same manner as the DA portion or alternately billed by using a calling card, billing to a third number, or collect. All operator-handled charges, as specified in 5.8, apply as appropriate.

There are no allowances for DACC, however, the Directory Assistance portion of the call is still governed by the appropriate call allowance as stated in Section 5.7.1.

For local and intraLATA calls, charges for DACC service are not applicable to calls placed by those customers with reading, visual, or physical handicaps.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.7 Directory Assistance Services, (Cont'd.)

5.7.3 National Directory Assistance Service

National Directory Assistance Service is provided to customers of the Company for the purpose of requesting telephone numbers of individuals or businesses who are located outside the customer's local Directory Assistance service area.

There are no call allowances or exemptions for National Directory Assistance.

A maximum of two(2) requested telephone numbers are allowed per call.

This service may be alternately billed by using a calling card, billing to a third number, or collect. Operator-handled charges, as specified in 5.8, apply as appropriate.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.7 Directory Assistance Services, (Cont'd.)

5.7.4 Maximum Rates

A. Basic Directory Assistance

Local Directory Assistance	Per query
Direct dialed (in excess of allowance)	$2.00
Via operator (no allowance)	$3.00

B. Directory Assistance Call Completion

Per completed call	$1.00

C. National Directory Assistance

Direct dialed	$2.00

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.8 Local Operator Service

The Company's operator services, available to presubscribed Customers, are accessible on a twenty-four (24) hour per day seven (7) days per week basis. In addition to the per call service charge, usage rates apply. The types of calls handled are as follows:

Customer Dialed Calling/Credit Card Call - This charge applies in addition to usage charges for station to station calls billed to an authorized Calling Card or Commercial Credit Card. The Customer must dial the destination telephone number where the capability exists for the Customer to do so. A separate rate applies in the event operator assistance is requested for entering the Customer's card number for billing purposes.

Operator Dialed Calling/Credit Card Call - This charge applies in addition to usage charges for station to station calls billed to an authorized telephone Calling Card or Commercial Credit Card and the operator dials the destination telephone number at the request of the Customer.

Operator Station - These charges apply in addition to usage charges for non-Person-to-Person calls placed using the assistance of a Company operator and billed Collect, to a Third Party, by deposit of coins in Pay Telephones, or via some method other than a Calling Card or Commercial Credit Card.

Person-to-Person - This charge applies in addition to usage charges for calls placed with the assistance of a Company operator to a particular party at the destination number. This charge applies regardless of billing method, including but not limited to billing to a Calling Card, Commercial Credit Card, Collect, by deposit of coins in Pay Telephones, or to a Third Party. Charges do not apply unless the specified party or an acceptable substitute is available.

Usage charges for local operator assisted calls are those usage charges that would normally apply to the calling party's service. In addition to usage charges, an operator assistance charge applies to each call.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.8 Local Operator Service, (Cont'd.)

5.8.1 Maximum Local and IntraLATA Per Call Service Charges:

Customer Dialed Calling Card	$4.50
Customer Dialed/Operator Assisted Calling Card	$6.05
Collect	$3.30
Third Party Billed	$3.30
Person-to-Person	$6.50

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.9 Busy Line Verification and Emergency Interrupt Service

Upon request of a calling party the Company will verify a busy condition on a designated local service line. The operator will determine if the line is clear or in use and report to the calling party. At the request of the Customer, the operator will interrupt the call on the busy line. Emergency Interruption is only permitted in cases where the calling party indicates an emergency exists and requests interruption. If the Customer has the operator interrupt a call, both the Busy Line Verification and the Emergency Interrupt charge will apply.

No charge will apply when the calling party advises that the call is to or from an official public emergency agency. Busy Verification and Interrupt Service is furnished where and to the extent that facilities permit.

The Customer shall identify and save the Company harmless against all claims that may arise from either party to the interrupted call or any person.

5.9.1 Maximum Rates

	Per call
Busy Line Verification, per request	$3.00
Emergency Interruption	$6.00

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.10 Directory Listing Service

5.10.1 General

The following rates and regulations apply to standard listings in light face type in the white pages (alphabetical section) of the telephone directory and to the Directory Assistance records of the Company.

Directory listings are limited to such information as is essential to the identification of the listed party. The listing of a service, commodity, or trade name is not permitted unless it is the name, or an integral part of the name, under which the Customer does business.

A listing is limited to one line in the directory, except where in the judgment of the Company, more than one line is required to identify the Customer properly. In such cases, the additional lines required are provided at no extra charge.

Listing services are available with all classes of main telephone exchange service.

5.10.2 Listings

A. Primary Listing

One listing, termed the primary listing, is included with each exchange access line or each joint user service.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.10 Directory Listing Service, (Cont'd.)

5.10.2 Listings, (Cont'd.)

B. Additional Listings

Additional listings may be the listings of individual names of those entitle to use the customer's service or , for business, Departments, Divisions, Tradenames, etc.

In connection with business and residence service, regular additional listings are available only in the names of Authorized Users of the Customer's service.

Ordinarily, all additional listings are of the same address and telephone number as the primary listings, except as provided for joint user and alternate number listings. However, when it appears necessary as an aid to the use of the directory and provided satisfactory service can be furnished, a listing will be permitted under the address of a branch exchange, Centrex or extension of an exchange service line installed on the premises of the Customer, but at an address different from that of the attendant position of main service.

Business additional listings are not permitted in connection with residence service. Residence additional listings are also permitted in connection with business service which is located in a residence and for permanent or season guests residing in a hotel or club.

A residence dual name additional listing is comprised of a surname, two first names, address and telephone number. A residence dual name additional listing may be provided for two persons who share the same surname and reside at the same address, or for a person known by two first names.

Special types of additional listings, such as Alternate, Alpha and Informational, Duplicate and Reference Listings, Foreign Listings, etc. take the same business or residence classification as the service with which such listings are furnished.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.10 Directory Listing Service, (Cont'd.)

5.10.2 Listings, (Cont'd.)

C. Nonpublished Service

The telephone numbers of nonpublished service are not listed in either the Company's alphabetical directory or Directory Assistance records available to the general public.

Non published information may be released to emergency service providers, to customers who subscribe to Company offerings which require the information to provide service and/ or bill their clients, or, to telephone customers who are billed for calls placed to or from nonpublished numbers and to entities which collect for the billed services. Nonpublished names and/or telephone numbers may also be delivered to customers on a call-by-call basis.

Incoming calls to nonpublished service will be completed by the Company only when the calling party places the call by number. The Company will adhere to this practice not withstanding any claim the calling party may present, except claims of emergencies involving life and death. In such cases, the Company will call the non-published number and request permission to make an immediate connection to the calling party.

When the Company agrees to keep a number unlisted, it does so without any obligation. Except for cases of gross negligence or willful misconduct, the Company is not liable for any damages that might arise from publishing a non-published number in the directory or disclosing it to some. If, in error, the telephone number is published in the directory, the Company's only obligation is to credit or refund any monthly charges the Customer paid for non-published service.

The Subscriber indemnifies (i.e., promises to reimburse the Company for any amount the Company must pay as a result of) and save the Company harmless against any and all claims for damages caused or claimed to have been caused, directly or indirectly, by the publication of a non-published service or the disclosing of said number to any person.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.10 Directory Listing Service, (Cont'd.)

5.10.2 Listings, (Cont'd.)

D. Nonlisted Service

Non-listed service means that the Customer's telephone number is not listed in the directory, but does it appear in the Company's Directory Assistance Records.

This service is subject to the rules and regulations for E911 service, where applicable.

The Company will only complete calls to a nonlisted number, if requested by a caller, during the course of a directory assistance call completion service.

When the Company agrees to keep a number unlisted, it does so without any obligation. Except for cases of gross negligence or willful misconduct, the Company is not liable for any damages that might arise from publishing a non-listed number in the directory or disclosing it to some. If, in error, the telephone number is listed in the directory, the Company's only obligation is to credit or refund any monthly charges the Customer paid for nonlisted service.

The subscriber indemnifies (i.e., promises to reimburse the Company for any amount the Company must pay as a result of) and save the Company harmless against any and all claims for damages caused or claimed to have been caused, directly or indirectly, by the publication of a non-listed service or the disclosing of said number to any person.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.10 Directory Listing Service, (Cont'd.)

5.10.2 Listings, (Cont'd.)

E. Toll-Free Directory Listings

Where available, a listing which references the Toll Free Number for a Business customer will be made available.

F. Straight Line Under Directory Listing

A business listing where one or more listings are indented under an original listing of the same customer without repetition of the name.

G. Caption and Subcaption Directory Listings

Two or more business listings may be placed under a caption consisting of the name of the customer or of any of the parties which the customer is entitled to list together with a designation or title where the name is not indicative of the business or profession. One or more sub captions may be furnished under a caption, each sub caption consisting of a directive heading which serves to identify two or more listings placed thereunder, where this grouping is necessary for the proper routing of calls.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.10 Directory Listing Service, (Cont'd.)

5.10.3 Maximum Rates and Charges

	Per Month
Primary Listings	$0.00
Change in Primary Listing	
Business, each	-----
Residence, each	-----
Additional Listings	
Business, each	$6.00
Residence, each	$3.00
Nonlisted Service	
Business, each	$3.00
Residence, each	$3.00
Nonpublished Service	
Business, each	$3.60
Residence, each	$3.80
Toll-Free Directory Listings	
Business, each	$30.00
Residence, each	N/A
Straight Line Under Listings	
Business, each	$10.00
Residence, each	N/A
Captions and Subcaptions Listings	
Business, each	$10.00
Residence, each	N/A

For non-recurring charges associated with a customer-initiated change in a directory listing, see Section 10.2.1 of this tariff.

Jon Brinton
President
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Phoenix, Arizona 85040

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.11 Carrier Presubscription

5.11.1 General

Carrier Presubscription is a procedure whereby a Customer designates to the Company the carrier which the Customer wishes to be the carrier of choice for intraLATA and interLATA toll calls. Such calls are automatically directed to the designated carrier, without the need to use carrier access codes or additional dialing to direct the call to the designated carrier. Presubscription does not prevent a Customer who has presubscribed to an IntraLATA or InterLATA toll carrier from using carrier access codes or additional dialing to direct calls to an alternative long distance carrier on a per call basis.

5.11.2 Presubscription Options - Customers may select the same carrier or separate carriers for intraLATA and interLATA long distance. The following options for long distance Presubscription are available:

Option A: Customer selects the Company as the presubscribed carrier for IntraLATA and InterLATA toll calls subject to presubscription.

Option B: Customer may select the Company as the presubscribed carrier for IntraLATA calls subject to presubscription and some other carrier as the presubscribed carrier for interLATA toll calls subject to presubscription.

Option C: Customer may select a carrier other than the Company for intraLATA toll calls subject to presubscription and the Company for interLATA toll calls subject to presubscription.

Option D: Customer may select the carrier other than the Company for both intraLATA and interLATA toll calls subject to presubscription.

Option E: Customer may select two different carriers, neither being the Company for intraLATA and interLATA toll calls. One carrier to be the Customer's primary intraLATA interexchange carrier. The other carrier to be the Customer's primary interLATA interexchange carrier.

Option F: Customer may select a carrier other than the Company for no presubscribed carrier for intraLATA toll calls subject to presubscription which will require the Customer to dial a carrier access code to route all intraLATA toll calls to the carrier of choice for each call.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.11 Carrier Presubscription, (Cont'd.)

5.11.3 Rules and Regulations

Customers of record will retain their primary interexchange carrier(s) until they request that their dialing arrangements be changed.

Customers of record or new Customers may select either Options A, B, C, D, E or F for intraLATA Presubscription.

Customers may change their selected Option and/or presubscribed toll carrier at any time subject to charges specified in 5.11.5 below:

5.11.4 Presubscription Procedures

A new Customer will be asked to select intraLATA and interLATA toll carriers at the time the Customer places an order to establish local exchange service with the Company. The Company will process the Customer's order for service. All new Customers' initial requests for intraLATA toll service presubscription shall be provided free of charge.

If a new Customer is unable to make selection at the time the new Customer places an order to establish local exchange service, the Company will read a random listing of all available intraLATA and interLATA carriers to aid the Customer in selection. If selection is still not possible, the Company will inform the Customer that he/she will be given 90 calendar days in which to inform the Company of his/her choice for primary toll carrier(s) free of charge. Until the Customer informs the Company of his/her choice of primary toll carrier, the Customer will not have access to long distance services on a presubscribed basis, but rather will be required to dial a carrier access code to route all toll calls to the carrier(s) of choice. Customers who inform the Company of a choice for toll carrier presubscription within the 90 day period will not be assessed a service charge for the initial Customer request.

Customers of record may initiate a intraLATA or interLATA presubscription change at any time, subject to the charges specified in 5.11.5 below. If a Customer of record inquires of the Company of the carriers available for toll presubscription, the Company will read a random listing of all available intraLATA carriers to aid the Customer in selection.

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.11 Carrier Presubscription, (Cont'd.)

5.11.5 Presubscription Charges

A. Application of Charges

After a Customer's initial selection for a presubscribed toll carrier and as detailed in above, for any change thereafter, an Presubscription Change Charge, as set for the below will apply. Customers who request a change in intraLATA and interLATA carriers with the same order will be assessed a single charge per line.

B. Maximum Nonrecurring Charges

Per business or residence line, trunk, or port: $10.00

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.12 Intercept Referral Service

5.12.1 General

Intercept Referral Service is a service used when a Customer disconnects service or changes telephone numbers. Calls to the intercepted telephone number are referred to an operator or a recorded message. Intercept services are offered for periods up to three (3) months for residential Customers and up to twelve (12) months for business Customers. Service is available subject to the availability of facilities and the disconnected number. The following Intercept services are available.

Basic Intercept Referral Service - Basic Intercept Service includes all intercept recordings that do not provide the new telephone number information.

New Number Referral Service - New Number Referral Service includes all intercept recordings that provide the new telephone number information.

Split Referral Intercept Service - Split Referral Intercept Service provides for calls to the disconnected number to be routed to the operator who will challenge the incoming call and provide the new number information dependent on the caller's response. The minimum billing period for this service is three months.

5.12.2 Maximum Rates

Basic Intercept Service is provided at no charge.

New Number Referral Service is provided at no charge.

Split Referral Intercept Service

	Business	Residence
Three months	$250.00	$80.00
Six months	$490.00	n/a
Nine months	$730.00	n/a
Twelve months	$980.00	n/a

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.13 Toll Restriction Service

Provides for Exchange Access lines or trunks to be restricted from dialing billable toll calls. Local directory assistance calls are allowed. This service is offered subject to the availability of facilities to individual line residence, individual line business and dial switching type customers. Provision of toll restriction does not alleviate customer responsibility for completed toll calls.

Toll Restriction may include Billed Number Screening (BNS) for residential customers. BNS prohibits collect and/or third number billed calls from being charged to BNS equipped numbers. Some calls, originating from locations that do not have screening capabilities, may not be capable of being intercepted and denied. These calls will be billed to the customer if completed.

5.13.1 Maximum Rates

	Residence	**Business**
Nonrecurring charge, per line	$12.00	$55.00
Monthly, per line	-----	$10.00

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.14 900 Service Access Restriction

900 Service Access Restriction enables residence or business exchange access line customers to prohibit dialing of calls with the 900 prefix. Customers who choose this service will also be restricted from calling calls with the prefix of 976 and 676. This service is offered only where facilities permit and is only available on direct dialed calls.

5.14.1 Maximum Rates

	Residence	**Business**
Nonrecurring charge, per line	$0.00	$0.00
Monthly rate, per line	$0.00	$0.00

SECTION 5.0 - MISCELLANEOUS SERVICES AND RATES, (CONT'D.)

5.15 Blocking for 10XXX1+/10XXX011+

This service prevents 10XXX1+ and 10XXX011+ calls from being completed and is offered subject to the availability of facilities. Provision of this service does not alleviate customer responsibility for completed toll calls.

5.15.1 Maximum Rates

	Nonrecurring Charge	Monthly Rate
Per line or trunk arranged	$6.00	$0.20

SECTION 6.0 - LONG DISTANCE SERVICES

6.1 General

Rates and regulations for the Company's Long Distance Services may be found in the Company's **Arizona Tariff No. 1.**

SECTION 7 – ADVANCED SERVICES

7.1 Direct Inward Dial (DID) Service

DID service is an optional feature which can be purchased in conjunction with Company-provided Basic Trunks or Digital Trunks. DID service transmits the dialed digits for all incoming calls allowing the Customer's PBX to route incoming calls directly to individual stations corresponding to each individual DID number. Charges for DID capability and DID numbers apply in addition to charges specified for Basic Trunks or Digital Trunks.

So the Company may efficiently manage its number resource, the Company, at its sole discretion, reserves the right to limit the quantity of DID numbers a Customer may obtain. Requests for 300 or more DID numbers must be provided to the Company in writing no less than five (5) months prior to activation. In addition, the Company reserves the right to review vacant DID stations or stations not in use to determine their utilization. Should the Company determine, based on its own discretion, that there is inefficient number utilization, the Company may reassign the DID numbers.

The Customer has no property right to the telephone number or any other call number destination associated with DID service furnished by the Company, and no right to the continuance of service through any particular end office. The Company reserves the right to change such numbers, or the end office designation associated with such numbers, or both, assigned to the Customer, whenever the Company deems it necessary to do so in the conduct of its business.

DID Numbers	Maximum Monthly Rates
Block of 20 DID Numbers	6.00
Individual DID Number	0.30
DID Trunk Termination	90.00

SECTION 7 – ADVANCED SERVICES

7.2 Advanced Service Packages

7.2.1 ISDN PRI Service with Unlimited Local Calling

ISDN PRI offers an array of value-added features, such as calling number identification and call-by-call selection that enhance productivity. ISDN PRI is configured with 23 64 Kbps bi-directional B (Bearer) channels and one 64 Kbps D (Data) channel. Unique to ISDN PRI is its ability to designate the D channel to handle all of the signaling and call control requirements and leave the remaining 23 B channels free for any mix of circuit-switched voice and data.

Each of these products is offered under a 12, 24 or 36 month term agreement. Rates include unlimited local calling for sent-paid, directly dialed calls. Rates do not include calling card calls, information type calls to Time and Weather, 555, 700, 900, 976 Services, Directory Assistance or any other type of Operator Handled call.

ISDN PRI includes the following non-optional Feature Package: Inbound Calling Line ID-Name & Number and Call by Call Selection.

Regional Toll and Long Distance Services must be PIC'd to the Company. These rates are in addition to ISDN PRI and DS1 rates below.

Recurring Charges

	Monthly Recurring Charge		
	12 Months	24 Months	36 Months
	ICB	ICB	ICB

Non-Recurring Charges

	Non-Recurring Charge		
	12 Months	24 Months	36 Months
First Line	ICB	ICB	ICB
Each Add'l Line	ICB	ICB	ICB

Expedite Service Charge[1]	Per PRI	
	ICB	
Order Supplement Charge[2]	First Change	Subsequent Change
Verizon	ICB	ICB
Order Cancellation Charge[Error! Bookmark not defined.]	Per PRI	
	ICB	

[1] Expedite Service Charges apply when customer requests installation of service in less time than normal installation interval of 30 business days.

[2] Order Supplement Charges apply when a change of the Requested Service Date is requested by customer. A change of requested service date must be within 30 days of the previous requested service date. In no event will the Company be obligated to accept more than three (3) changes to a requested service date. The service will be deemed canceled upon the fourth (4) such request and applicable Order Cancellation Charges will apply.

SECTION 7 – ADVANCED SERVICES

7.2 Advanced Service Packages, (Cont'd.)

7.2.2 Digital DS-1 PBX Service with Unlimited Local Calling

This service provides a trunk side DS1 electrical interface from the customer's digital PBX system to a digital port on a local Company switch for the origination and termination of calls. Traffic to and from the digital PBX can be received or dialed directly from any PBX station without the need for an attendant.

These digital trunks deliver a high-speed DS1 (T1) connection between your PBX and the Company network. There are up to 24 channels on one facility, each of which can be used to place or receive calls. This multi-channel capability dramatically reduces the need for additional PBX circuit cards.

Each of these products is offered under a 12, 24 or 36 month term agreement. Rates include unlimited local calling for sent-paid, directly dialed calls. Rates do not include calling card calls, information type calls to Time and Weather, 555, 700, 900, 976 Services, Directory Assistance or any other type of Operator Handled call.

Regional Toll and Long Distance Services must be PIC'd to the Company. These rates are in addition to ISDN PRI and DS1 rates below.

Monthly Recurring Charges

Monthly Recurring Charge		
12 Months	24 Months	36 Months
ICB	ICB	ICB

Non-Recurring Charges

	Non-Recurring Charge		
	12 Months	24 Months	36 Months
First Line	ICB	ICB	ICB
Each Add'l Line	ICB	ICB	ICB

Expedite Service Charge[3]	Per DS1	
SBC/Pacific Bell	ICB	
Order Supplement Charge[4]	First Change	Subsequent Change
	ICB	ICB
Order Cancellation Charge Error! Bookmark not defined.	Per DS1	
	ICB	

[3] Expedite Service Charges apply when customer requests installation of service in less time than normal installation interval of 30 business days.

[4] Order Supplement Charges apply when a change of the Requested Service Date is requested by customer. A change of requested service date must be within 30 days of the previous requested service date. In no event will the Company be obligated to accept more than three (3) changes to a requested service date. The service will be deemed canceled upon the fourth (4) such request and applicable Order Cancellation Charges will apply.

SECTION 7 – ADVANCED SERVICES

7.2 Advanced Service Packages, (Cont'd.)

7.2.3 ISDN PRI Service with Unlimited Local Calling and Bundled Toll/LD Service

ISDN PRI offers an array of value-added features, such as calling number identification and call-by-call selection that enhance productivity. ISDN PRI is configured with 23 64 Kbps bi-directional B (Bearer) channels and one 64 Kbps D (Data) channel. Unique to ISDN PRI is its ability to designate the D channel to handle all of the signaling and call control requirements and leave the remaining 23 B channels free for any mix of circuit-switched voice and data.

This product is offered under a 12, 24 or 36 month term agreement. Rates include unlimited local calling for sent-paid, directly dialed calls. Rates do not include calling card calls, information type calls to Time and Weather, 555, 700, 900, 976 Services, Directory Assistance or any other type of Operator Handled call.

The Unlimited Local Calling and Bundled Toll/LD Service Products are offered with six different increments of Toll/LD Minutes of Use: 5,000, 10,000, 15,000, 30,000, 50,000 and 100,000. Installation charges are included in the monthly recurring charges. Regional Toll and Long Distance Services must be PIC'd to the Company.

<u>ISDN PRI with Unlimited Local and Bundled 5,000 Long Distance MOU</u>
This package includes unlimited local and 5,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 5,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

	Monthly Recurring Charge	
12 Months	24 Months	36 Months
ICB	ICB	ICB

<u>ISDN PRI with Unlimited Local and Bundled 10,000 Long Distance MOU</u>
This package includes unlimited local and 10,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 10,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

	Monthly Recurring Charge	
12 Months	24 Months	36 Months
ICB	ICB	ICB

SECTION 7 – ADVANCED SERVICES

7.2 Advanced Service Packages, (Cont'd.)

7.2.3 ISDN PRI Service with Unlimited Local Calling and Bundled Toll/LD Service, (Cont'd.)

ISDN PRI with Unlimited Local and Bundled 15,000 Long Distance MOU
This package includes unlimited local and 15,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 15,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

	Monthly Recurring Charge		
	12 Months	24 Months	36 Months
	ICB	ICB	ICB

ISDN PRI with Unlimited Local and Bundled 30,000 Long Distance MOU
This package includes unlimited local and 30000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 30,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

	Monthly Recurring Charge		
	12 Months	24 Months	36 Months
SBC/Pacific Bell Area	ICB	ICB	ICB

ISDN PRI with Unlimited Local and Bundled 50,000 Long Distance MOU
This package includes unlimited local and 50,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 50,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

	Monthly Recurring Charge		
	12 Months	24 Months	36 Months
	ICB	ICB	ICB

ISDN PRI with Unlimited Local and Bundled 100,000 Long Distance MOU
This package includes unlimited local and 100,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number & Call-by-Call Selection (ISDN PRI) long distance usage @ 100,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

	Monthly Recurring Charge		
	12 Months	24 Months	36 Months
	ICB	ICB	ICB

SECTION 7 – ADVANCED SERVICES

7.2 Advanced Service Packages, (Cont'd.)

7.2.4 Digital DS-1 PBX Service with Unlimited Local Calling and Bundled Toll/LD Service

This service provides a trunk side DS1 electrical interface from the customer's digital PBX system to a digital port on a local Company switch for the origination and termination of calls. Traffic to and from the digital PBX can be received or dialed directly from any PBX station without the need for an attendant.

These digital trunks deliver a high-speed DS1 (T1) connection between your PBX and the Company network. There are up to 24 channels on one facility, each of which can be used to place or receive calls. This multi-channel capability dramatically reduces the need for additional PBX circuit cards.

Each of these products is offered under a 12, 24 or 36 month term agreement. Rates include unlimited local calling for sent-paid, directly dialed calls. Rates do not include calling card calls, information type calls to Time and Weather, 555, 700, 900, 976 Services, Directory Assistance or any other type of Operator Handled call.

The Digital DS-1 PBX Service with Unlimited Local Calling and Bundled Toll/LD Service Products are offered with six different increments of Toll/LD Minutes of Use: 5,000, 10,000, 15,000, 30,000, 50,000 and 100,000. Installation charges are included in the monthly recurring charges. Regional Toll and Long Distance Services must be PIC'd to the Company.

<u>ISDN DS1 with Unlimited Local and Bundled 5,000 Long Distance MOU</u>
This package includes unlimited local and 5,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 5,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

Monthly Recurring Charge		
12 Months	24 Months	36 Months
ICB	ICB	ICB

<u>ISDN DS1 with Unlimited Local and Bundled 10,000 Long Distance MOU</u>
This package includes unlimited local and 10,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 10,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

Monthly Recurring Charge		
12 Months	24 Months	36 Months
ICB	ICB	ICB

SECTION 7 – ADVANCED SERVICES

7.2 Advanced Service Packages, (Cont'd.)

7.2.4 Digital DS-1 PBX Service with Unlimited Local Calling and Bundled Toll/LD Service, (Cont'd.)

ISDN DS1 with Unlimited Local and Bundled 15,000 Long Distance MOU
This package includes unlimited local and 15,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 15,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

Monthly Recurring Charge		
12 Months	24 Months	36 Months
ICB	ICB	ICB

ISDN DS1 with Unlimited Local and Bundled 30,000 Long Distance MOU
This package includes unlimited local and 30000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 30,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

Monthly Recurring Charge		
12 Months	24 Months	36 Months
ICB	ICB	ICB

ISDN DS1 with Unlimited Local and Bundled 50,000 Long Distance MOU
This package includes unlimited local and 50,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 50,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

Monthly Recurring Charge		
12 Months	24 Months	36 Months
ICB	ICB	ICB

ISDN DS1 with Unlimited Local and Bundled 100,000 Long Distance MOU
This package includes unlimited local and 100,000 long distance minutes of use. Also included is Inbound Calling Line ID-Name & Number and long distance usage @ 100,000 MOUs (including regional toll). Usage over the selected LD package will be billed at $0.049 per minute.

Monthly Recurring Charge		
12 Months	24 Months	36 Months
ICB	ICB	ICB

SECTION 7 – ADVANCED SERVICES

7.2 Advanced Service Packages, (Cont'd.)

7.2.5 ISDN BRI Service

ISDN BRI (Basic Rate Interface) uses standard "twisted pair" cables and is nearly three times faster than a 56K dial up line. ISDN PRI (Primary Rate Interface) uses a 1.544 Mbps digital transport facility (T1). Both services provide the superior clarity of digital transmission, a high-speed data interface and sufficient bandwidth capacity to fulfill your current and future communication needs.

ISDN BRI consists of two 64 Kbps B (Bearer) channels and one 16 Kbps D (Data) channel. Each B channel has the ability to integrate voice, data, image and video. The B channels may be kept separate or bonded together to deliver 128 Kbps.

Monthly Recurring Charges

		Monthly Recurring Charge[5]
ISDN Basic Exchange Digital Line, each		$10.00
ISDN Basic Exchange Circuit Switched Voice		
	First Line	n/a
	Second Line	2.00
ISDN Basic Exchange Circuit Switched Data, each		2.00
ISDN Basic Exchange Alternate Circuit Switched Voice/Data,each		2.00

[5] These ISDN BRI rates are a supplement to individual Message Rate Service.

SECTION 7 – ADVANCED SERVICES

7.2 Advanced Service Packages, (Cont'd.)

7.2.6 Digital Centrex Service

Digital Centrex Service delivers superior performance, PBX-like functionality including abbreviated dialing, and is compatible with many telephone sets. Each user has a unique seven-digit direct telephone number and customized features. The service is affordable, power failure safe and provides a scalable platform for future growth and technology.

Monthly Recurring Charges

Contract Length	Monthly Recurring Charge
12 months – Assume Dial 9	26.61
12 months	23.15
24 months	21.05
36 months	17.59
60 months	16.51
84 months	15.80

NOTES FOR ALL ADVANCED SERVICES: Availability of services must be verified with the Company based on customer address and NPA-NXX. Rates do not included FCC End User Charge, FCC Port Charge, or other surcharges and taxes. Minimum service period is 12 months. If service is cancelled prior to the end of the contract, a termination charge will be calculated as follows: a. The average of the sum of all line charges on three previous Company invoices to the customer (excluding taxes) multiplied by the number of months remaining in the term agreement.

SECTION 8 - SPECIAL ARRANGEMENTS

8.1 Individual Case Basis (ICB) Arrangements

Arrangements will be developed on a case-by-case basis in response to a bona fide special request from a Customer or prospective Customer to develop a competitive bid for a service not generally offered under this tariff. Rates quoted in response to such competitive requests may be different than those specified for such services in this tariff. ICB rates will be offered to the Customer in writing and on a nondiscriminatory basis.

ICB will be filed with the Communications Division of the Commission.

SECTION 9 - PROMOTIONAL OFFERINGS

9.1 Special Promotions

The Company may, from time to time, offer services in this Tariff at special promotional rates and/or terms. Such promotional arrangements shall be filed with the Commission when so required. All rates and terms contained in this Tariff shall continue to apply unless specifically addressed in the promotional agreements.

SECTION 10 - CURRENT PRICE LIST

10.1 Basic Services and Rates

10.1.1 Network Exchange Bundled Service

A. Arizona Home Edition - Standard Service

Arizona Home Edition will be provided at the following rates:

	MONTHLY RATE
• Per individual flat rate residence line with three features	$12.81
• Per additional flat rate residence line with three features	15.99

B. Arizona Home Edition - Deluxe Service

Arizona Deluxe Edition will be provided at the following rates:

	MONTHLY RATE
• Per individual flat rate residence line with three features	$19.81
• Per additional flat rate residence line with three features	22.99

SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.1 Basic Services and Rates, (Cont'd.)

10.1.1 Network Exchange Bundled Service, (Cont'd.)

D. Business A La Carte Service

Business A La Carte service is targeted at small business Customers and provides options based on the Customers calling patterns and estimated usage. Customers who subscribe to this service must designate Inter-Tel as the presubscribed carrier for local calling concurrent with enrollment for this service. Business A La Carte provides Customers with the option of selecting Inter-Tel for toll services.

Local Exchange Service

Local Access Line

Local Business Line	
Monthly Rate, per line	$30.40
Service Connection Fee, one-time charge per line*	
Per Line	$42.50
PBX Trunk	
Monthly Rate	$38.51
Service Connection Fee, one-time charge per line*	
Per Line	$56.00

* Service Connection fee is waived for those customers who retain their existing telephone number when switching their service to Inter-Tel. The charge will apply if additional lines are transferred to Inter-Tel after the initial order.

* Service Connection fee is waived for those customers who retain their existing telephone number when switching their service to Inter-Tel. The charge will apply if additional lines are transferred to Inter-Tel after the initial order.

SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.1 Basic Services and Rates, (Cont'd.)

10.1.1 Network Exchange Bundled Service, (Cont'd.)

D. Arizona Business Edition - Standard Service

Arizona Business Edition - Standard Service will be provided at the following rate:

	MONTHLY RATE
Per individual or additional flat rate business line	$39.99

E. Arizona Business Edition - Deluxe Service

Arizona Business Edition - Deluxe will be provided at the following rate:

	MONTHLY RATE
Per individual or additional flat rate business line	$49.99

SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.1 Basic Services and Rates, (Cont'd.)

10.1.2 Direct Inward Dial (DID) Service

	Monthly Recurring
DID Numbers	
Block of 20 DID Numbers	3.00
Individual DID Number	0.15
DID Trunk Termination	45.00

10.1.3 Advanced Services

RESERVED FOR FUTURE USE

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SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.2 Miscellaneous Services and Rates

10.2.1 Service Order and Change Charges

Non-recurring charges apply to processing Service Orders for new service and for changes in service.

	Residence	Business
Service Order Charges		
Primary and Secondary Service Connection Charge*	$27.50	$42.50
Transfer of Service Charge, Primary Line	$89.99	$49.99
Transfer of Service Charge, Secondary Line	$75.00	$49.99
Technician Dispatch Charge (or Trouble Isolation Charge)	$69.99	$79.99
Service Order Charge	10.00	22.00
Premises Visit Charge, first 15 minutes	60.00	60.00
Premises Visit Charge, add'l 15 minutes	30.00	30.00
Change Order Charges:		
Telephone Number Change Order	$10.00	$10.00
Feature or Feature Pack Change Order	$10.00	$10.00
Toll Restriction Fee Order	$10.00	$10.00
Listing Change Charge	$10.00	$10.00
Home Edition Change Charge	$10.00	$10.00
Record Change Charges:		
Record Order Charge	8.50	22.00
Miscellaneous Charges		
Duplicate Invoice	$5.00	$5.00
Call Detail Report	$5.00	$5.00

* This charge not applicable where a Service Connection Fee is listed for a specific service such as Network Bundled Service. See Section 10.1.1 for Network Bundled Service nonrecurring charges.

SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.2 Miscellaneous Services and Rates, (Cont'd.)

10.2.2 RESERVED FOR FUTURE USE

SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.2 Miscellaneous Services and Rates, (Cont'd.)

10.2.3 Restoration of Service

	Residence	Business
Per occasion, per line	$25.00	$55.00

10.2.4 Temporary Suspension/Restoration of Service

	Residence	Business
Nonrecurring charge, per line suspended	$10.00	$27.50
Recurring charge, per line suspended	50% of regular service rates	
Nonrecurring charge, per line restored	$10.00	$27.50

10.2.5 Public Telephone Surcharge

Rate Per Call: $0.75

SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.2 Miscellaneous Services and Rates, (Cont'd.)

10.2.6 Optional Calling Features

	Residential	Business
FEATURE	**Monthly**	**Monthly**
Speed Calling		
8 Number	1.75	2.50
30 Number	2.50	4.00
Call Forwarding		
Variable	2.50	4.30
Busy Line (Expanded)	0.30	2.50
Busy Line (Overflow)	0.30	4.00
Busy Line (Programmable)	1.60	7.50
Don't Answer	0.65	3.50
Don't Answer (Expanded)	0.65	3.50
Don't Answer (Programmable)	2.10	4.00
Busy Line/Don't Answer	0.85	5.00
Busy Line (External)/DA	0.85	5.00
Call Rejection	4.00	4.00
Call Waiting	2.50	7.00
Call Transfer	5.50	5.50
Caller ID		
Name and Number	5.00	7.45
Number	5.00	7.45
Continuous Redial	2.25	3.00
Distinctive Alert	0.08	0.75
Hot Line	1.75	1.75
Priority Call	2.25	3.00
Remote Access Forwarding	3.45	7.25
Selective Call Forwarding	2.25	3.00

Per Use Features

	Residential		Business	
FEATURE	**Per Use**	**Monthly**	**Per Use**	**Monthly**
Call Tracing - per use	$2.00	N/A	$2.00	N/A
Repeat Call - per use	$0.75	$2.25	$0.75	$3.00
Return Call - per use	$0.75	$2.70	$0.75	$2.50
Three-Way Calling, per use	$0.75	$2.50	$0.75	$3.50

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SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.2 Miscellaneous Services and Rates, (Cont'd

10.2.7 Directory Assistance Services

A. Basic Directory Assistance

Local Directory Assistance	Per query
Direct dialed (in excess of allowance)	$1.15
Via operator (no allowance)	$1.50

B. Directory Assistance Call Completion

Per completed call	$0.50

C. National Directory Assistance

Direct dialed	$1.50

SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.2 Miscellaneous Services and Rates, (Cont'd.)

10.2.8 Local Operator Service

Local and IntraLATA Per Call Service Charges:

Customer Dialed Calling Card	$2.00
Customer Dialed/Operator Assisted Calling Card	$3.00
Collect	$1.30
Third Party Billed	$1.30
Person-to-Person	$3.50

10.2.9 Busy Line Verification and Emergency Interrupt Service

	<u>Per call</u>
Busy Line Verification, per request	$2.25
Emergency Interruption	$3.00

SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.2 Miscellaneous Services and Rates, (Cont'd.)

10.2.10 Directory Listing Service

	Per Month
Primary Listings	$0.00
Change in Primary Listing	
Business, each	-----
Residence, each	-----
Additional Listings	
Business, each	$2.50
Residence, each	$1.25
Nonlisted Service	
Business, each	$1.20
Residence, each	$1.30
Nonpublished Service	
Business, each	$1.55
Residence, each	$1.65
Toll-Free Directory Listings, each	
Business, each	$15.00
Residence, each	N/A
Straight Line Under Listings	
Business, each	$2.00
Residence, each N/A	
Captions and Subcaptions Listings	
Business, each	$2.00
Residence, each	N/A

For non-recurring charges associated with a customer-initiated change in a directory listing, see Section 10.2.1 of this tariff.

SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.2 Miscellaneous Services and Rates, (Cont'd.)

10.2.11 Carrier Presubscription

Nonrecurring Charges

Per business or residence line, trunk, or port: $5.00

10.2.12 Intercept Referral Service

Basic Intercept Service is provided at no charge.

New Number Referral Service is provided at no charge.

Split Referral Intercept Service

	Business	**Residence**
Three months	$125.00	$40.00
Six months	$245.00	n/a
Nine months	$365.00	n/a
Twelve months	$490.00	n/a

SECTION 10.0 - CURRENT PRICE LIST, (CONT'D.)

10.2 Miscellaneous Services and Rates, (Cont'd.)

10.2.13 Toll Restriction Service

	Residence	Business
Nonrecurring charge, per line	$6.00	$27.50
Monthly, per line	-----	$5.00

10.2.14 900 Service Access Restriction

	Residence	Business
Nonrecurring charge, per line	$0.00	$0.00
Monthly rate, per line	$0.00	$0.00

10.2.15 Blocking for 10XXX1+/10XXX011+

	Nonrecurring Charge	Monthly Rate
Per line or trunk arranged	$3.00	$0.10

10.2.16 Returned Check Charge

Per dishonored check returned $25.00

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C - Legal Notice

Will be submitted when Docket No. Assigned by Commission.

D - Financial Information

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

FORM 10-Q
QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarter ended March 31, 2005	Commission File Number: 0-10211

INTER-TEL, INCORPORATED

Incorporated in the State of Arizona I.R.S. No. 86-0220994

1615 S. 52nd Street
Tempe, Arizona 85281

(480) 449-8900

Title of Class	Outstanding as of March 31, 2005
Common Stock, no par value	26,709,745

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 periods that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes ☑ No ☐

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INTER-TEL, INCORPORATED AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS
INTER-TEL, INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share amounts)	March 31, 2005 (Unaudited)	December 31, 2004 (Note A)
ASSETS		
CURRENT ASSETS		
Cash and equivalents	$ 125,824	$ 152,330
Short-term investments	55,314	52,644
TOTAL CASH AND SHORT-TERM INVESTMENTS	181,138	204,974
Accounts receivable, net of allowances of $9,442 in 2005 and $9,921 in 2004	42,938	45,176
Inventories	19,299	16,055
Net investment in sales-leases, net of allowances of $861 in 2005 and $886 in 2004	18,160	17,151
Income taxes receivable	6,102	4,017
Deferred income taxes	11,651	9,905
Prepaid expenses and other assets	8,706	7,194
TOTAL CURRENT ASSETS	287,994	304,472
LONG-TERM INVESTMENTS	5,900	9,900
PROPERTY, PLANT & EQUIPMENT	28,848	27,840
GOODWILL	26,460	19,890
PURCHASED INTANGIBLE ASSETS	26,870	10,987
NET INVESTMENT IN SALES-LEASES, net of allowances of $1,960 in 2005 and $1,810 in 2004	35,781	33,877
TOTAL ASSETS	$ 411,853	$ 406,966
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 32,274	$ 30,801
Accrued dividends payable on common stock	28,846	1,829
Other current liabilities	42,960	50,367
TOTAL CURRENT LIABILITIES	104,080	82,997
DEFERRED TAX LIABILITY	65,975	65,234
LEASE RECOURSE LIABILITY	12,721	12,241
OTHER LIABILITIES	7,018	7,063
SHAREHOLDERS' EQUITY		
Common stock, no par value-authorized 100,000,000 shares; issued–27,161,823 shares; outstanding–26,709,745 at March 31, 2005 and 26,125,799 shares at December 31, 2004	119,933	116,598
Retained earnings	106,240	134,455
Accumulated other comprehensive income	1,388	924
	227,561	251,977
Less: Treasury stock at cost – 452,078 shares at March 31, 2005 and 1,036,024 shares at December 31, 2004	(5,502)	(12,546)
TOTAL SHAREHOLDERS' EQUITY	222,059	239,431
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 411,853	$ 406,966

See accompanying notes.

INTER-TEL, INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

(In thousands, except per share amounts)	Three Months Ended March 31, 2005	2004
NET SALES		
Telecommunications systems, software and related	$ 92,659	$86,049
Resale of local, long distance and network services	13,048	11,982
TOTAL NET SALES	105,707	98,031
COST OF SALES		
Telecommunications systems, software and related	43,397	38,875
Resale of local, long distance and network services	8,256	7,058
TOTAL COST OF SALES	51,653	45,933
GROSS PROFIT	54,054	52,098
Research and development	8,455	6,035
Selling, general and administrative	38,723	35,004
Amortization of purchased intangible assets	762	445
Write-off of in-process research and development costs	2,600	—
	50,540	41,484
OPERATING INCOME	3,514	10,614
Interest and other income	947	506
Foreign currency transaction gains (losses)	53	(161)
Interest expense	(23)	(46)
INCOME BEFORE INCOME TAXES	4,491	10,913
INCOME TAXES	2,556	4,093
NET INCOME	$ 1,935	$ 6,820
NET INCOME PER SHARE — BASIC	$ 0.07	$ 0.27
NET INCOME PER SHARE — DILUTED	$ 0.07	$ 0.25
DIVIDENDS PER SHARE	$ 1.08	$ 0.07
Average number of common shares outstanding — Basic	26,373	25,543
Average number of common shares outstanding — Diluted	27,788	27,350

See accompanying notes.

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INTER-TEL, INCORPORATED AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

(In thousands)	Three Months Ended March 31, 2005	2004
OPERATING ACTIVITIES		
Net income	$ 1,935	$ 6,820
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation of fixed assets	2,253	1,881
Amortization of patents included in R&D expenses	55	55
Amortization of purchased intangible assets	762	445
Purchased in-process research and development	2,600	
Provision for losses on receivables	481	429
Provision for losses on leases	769	1,045
Provision for inventory valuation	243	191
Decrease in other liabilities	(165)	(996)
Loss on sale of property and equipment	19	—
Deferred income taxes	494	4,928
E-Rate settlement	(8,461)	—
Changes in operating assets and liabilities	(3,392)	1,122
NET CASH (USED IN) PROVIDED BY OPERATING ACTIVITIES	(2,407)	15,920
INVESTING ACTIVITIES		
Purchases of short-term investments	(10,269)	(19,989)
Maturities and sales of short-term investments	11,599	22,383
Additions to property, plant and equipment	(2,218)	(1,219)
Proceeds from disposal of property, plant and equipment	4	8
Cash used in acquisitions	(27,579)	—
NET CASH (USED IN) PROVIDED BY INVESTING ACTIVITIES	(28,463)	1,183
FINANCING ACTIVITIES		
Cash dividends paid	(1,829)	(1,525)
Payments on term debt	(11)	(17)
Proceeds from exercise of stock options	5,740	3,240
NET CASH PROVIDED BY FINANCING ACTIVITIES	3,900	1,698
EFFECT OF EXCHANGE RATE CHANGES	464	292
INCREASE (DECREASE) IN CASH AND EQUIVALENTS	(26,506)	19,093
CASH AND EQUIVALENTS AT BEGINNING OF PERIOD	152,330	115,197
CASH AND EQUIVALENTS AT END OF PERIOD	$125,824	$134,290

See accompanying notes.

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INTER-TEL, INCORPORATED AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)
March 31, 2005

NOTE A—BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with U.S. generally accepted accounting principles applicable to interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation of the results for the interim periods presented have been included. Operating results for the quarter ending March 31, 2005 are not necessarily indicative of the results that may be expected for the year ended December 31, 2005. The balance sheet at December 31, 2004 has been derived from the audited financial statements at that date, but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. For further information, refer to the consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2004.

Certain prior year amounts have been reclassified to conform with the current period presentation.

Stock-Based Compensation

In 2002, the Financial Accounting Standards Board ("FASB") issued Statement No. 148 "Accounting for Stock-Based Compensation—Transition and Disclosure, an amendment of FASB Statement No. 123" ("SFAS No. 148"), which provides alternative methods of transition for an entity that voluntarily changes to the fair value based method of accounting for stock-based employee compensation. It also amends the disclosure provisions of SFAS No. 123 to require prominent disclosure about the effects on reported net income of an entity's accounting policy decisions with respect to stock-based employee compensation. Finally, this statement amends APB Opinion No. 28, "Interim Financial Reporting," to require disclosure about those effects in interim financial information. We adopted SFAS No. 148 in the fourth quarter of 2002. Since we have not changed to a fair value method of stock-based compensation, the applicable portion of this statement only affects our footnote disclosures.

We do not recognize compensation expense relating to employee stock options because we only grant options with an exercise price equal to the fair value of the stock on the effective date of grant. At March 31, 2005, the Company has four stock-based employee and director incentive plans and an employee stock purchase plan. The Company accounts for these plans under the recognition and measurement principles of APB No. 25, "Accounting for Stock Issued to Employees," and related interpretations. Stock-based employee compensation costs are not reflected in net income, as all options granted under the plans had an exercise price equal to the market value of the underlying common stock on the date of grant. If we had elected to recognize compensation expense using a fair value approach, and therefore determined the compensation based on the value as determined by the modified Black-Scholes option pricing model, the pro forma net income and earnings per share would have been as follows:

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(In thousands, except per share amounts)	Three Months Ended March 31, 2005	2004
Net income, as reported	$1,935	$6,820
Deduct: total stock-based compensation expense, determined under fair value based method for all awards, net of tax	(859)	(783)
Pro forma net income	$1,076	$6,037
Earnings per share of common stock:		
Basic -- as reported	$ 0.07	$ 0.27
Basic -- pro forma	$ 0.04	$ 0.24
Diluted -- as reported	$ 0.07	$ 0.25
Diluted -- pro forma	$ 0.04	$ 0.22

Pro forma results disclosed are based on the provisions of SFAS 123 using the Black-Scholes option valuation model and are not likely to be representative of the effects on pro forma net income for future years. In addition, the Black-Scholes option valuation model was developed for use in estimating the fair value of traded options, which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because our stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in our opinion, the estimating models do not necessarily provide a reliable single measure of the fair value of our stock options. The option pricing model utilized the following weighted average assumptions for 2005 and 2004: risk free interest rates of 3.73% for 2005 and 2.81% for 2004; dividend yields of 1.31% for 2005 and 0.82% for 2004; volatility factors of the expected market price of our stock averaged 0.45 for 2005 and 0.46 for 2004. Employee stock options granted through March 31, 2005 vest over four to five year periods and director options vest at the end of six months from the grant date.

On April 26, 2005, the Compensation Committee of the Board of Directors of Inter-Tel, with the approval of the board of directors, approved the acceleration of the vesting of certain unvested stock options previously granted to employees under the Company's 1994 Long Term Incentive Plan, 1997 Long Term Incentive Plan and the Acquisition Stock Option Plan. With the exception of any options granted to all Directors and Named Executive Officers, all unvested options with exercise prices greater than the closing price as of the close of the Nasdaq stock market on May 3, 2005 ($19.13) became exercisable in full. Such options would otherwise have vested from time to time over the next five years. Approximately 617,000 options were accelerated at grant prices ranging from $19.16 to $31.58. All other terms and conditions applicable to outstanding stock option grants, including the exercise prices and number of shares subject to the accelerated options, were unchanged. The stock option agreements with respect to the options will be amended accordingly.

The Board of Directors considered several factors in determining to accelerate the vesting of these options, including the effect on the Company's reported stock option expense in future periods, administrative burden required to track and account for the vesting periods under new accounting rules and the potential benefit to the Company and its shareholders in retaining the services of the affected employees. As currently drafted, Statement of Financial Accounting Standards No. 123 (Revised 2004) or SFAS 123R will require the Company to treat unvested stock options as an expense effective with the fiscal quarter ending March 31, 2006.

Contingencies

We are a party to various claims and litigation in the normal course of business. Management's current estimated range of liability related to various claims and pending litigation is based on claims for which our management can estimate the amount and range of loss. Because of the uncertainties related to both the amount and range of loss on the remaining pending claims and litigation, management is unable to make a reasonable estimate of the liability that could result from an unfavorable outcome. As

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additional information becomes available, we will assess the potential liability related to our pending litigation and revise our estimates. Such revisions in our estimates of the potential liability could materially impact our results of operations and financial position.

On January 5, 2005, the Company received court approval of a civil settlement agreement (the "Civil Settlement") and a criminal plea agreement (the "Plea Agreement") with the United States of America, each dated as of December 8, 2004 and disclosed on that same date. The court approval of the Civil Settlement and Plea Agreement resolves the investigation of the Department of Justice into the participation of Inter-Tel Technologies, Inc., the Company's wholly-owned subsidiary ("Technologies") in a federally administered "E-Rate program" to connect schools and libraries to the Internet. In connection with the Civil Settlement, Technologies agreed to pay a penalty of $6,740,450 and forego the collection of certain accounts receivable of $259,540 related to Technologies' participation in the E-Rate program. In connection with the Plea Agreement, Technologies entered guilty pleas to charges of mail fraud and an antitrust violation. Under the Plea Agreement, Technologies agreed to pay a fine of $1,721,000 and observe a three-year probationary period, which will, among other things, require Technologies to implement a comprehensive corporate compliance program. The penalties and fines described above were paid during the first quarter of 2005.

In addition, on January 21, 2005, Inter-Tel Technologies received notification from the Federal Communications Commission that Technologies was temporarily suspended from participation in the E-Rate program pending a proposed debarment. Technologies has contested the scope and length of the proposed debarment from the E-Rate program, but there can be no assurance that Technologies will be successful in this regard. Revenues in 2004 relating to Technologies' participation in the E-Rate program were not significant.

The existence and disclosure of the Civil Settlement, Plea Agreement and FCC Notice may have already caused competitive harm to Inter-Tel, and these matters may further harm Inter-Tel's business.

Inventories

We value our inventories at the lower of cost (principally on a standard cost basis, which approximates the first-in, first-out (FIFO) method) or market.

Recent Accounting Pronouncements

In December 2004, the FASB issued SFAS No. 123R *"Share Based Payment."* This statement is a revision to SFAS No. 123, supersedes APB No. 25, *"Accounting for Stock Issued to Employees,"* and amends SFAS No. 95, *"Statement of Cash Flows."* This statement will require us to expense the cost of employee services received in exchange for an award of equity instruments. This statement also provides guidance on valuing and expensing these awards, as well as disclosure requirements, and is effective for Inter-Tel for the first interim reporting period that begins January 1, 2006. SFAS No. 123R permits public companies to choose between the following two adoption methods:

1. A "modified prospective" method in which compensation cost is recognized beginning with the effective date (a) based on the requirements of SFAS No. 123R for all share-based payments granted after the effective date and (b) based on the requirements of SFAS No. 123 for all awards granted to employees prior to the effective date of SFAS No. 123R that remain unvested on the effective date, or

2. A "modified retrospective" method which includes the requirements of the modified prospective method described above, but also permits entities to restate based on the amounts previously recognized under SFAS No. 123 for purposes of pro forma disclosures either (a) all prior periods presented or (b) prior interim periods of the year of adoption.

As permitted by SFAS No. 123, we currently account for share-based payments to employees using the APB No. 25 intrinsic value method and recognize no compensation cost for employee stock options or the employee stock purchase plan shares. As proposed, companies would be required to recognize an expense for compensation costs related to share-based payment arrangements, including stock options

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and employee stock purchase plans. The impact of the adoption of SFAS No. 123R cannot be predicted at this time because it will depend on levels of share-based payments granted in the future. However, valuation of employee stock options under SFAS No. 123R is similar to SFAS No. 123, with some exceptions. For information about what our reported results of operations and earnings per share would have been had we adopted SFAS No. 123, see the table above under the heading "Stock Based Compensation." The adoption of SFAS No. 123R's fair value method will have a significant impact on our results of operations, although it will have no impact on our overall financial position. Due to timing of the release of SFAS No. 123R, we have not yet completed the analysis of the ultimate impact that this new pronouncement will have on the results of operations, nor the method of adoption for this new standard.

NOTE B—EARNINGS PER SHARE

Diluted earnings per share assume that outstanding common shares were increased by shares issuable upon the exercise of all outstanding stock options for which the market price exceeds exercise price, less shares which could have been purchased with related proceeds, if the effect would not be antidilutive.

The following table sets forth the computation of basic and diluted earnings per share:

(In thousands, except per share amounts)	Three Months Ended March 31, 2005	Three Months Ended March 31, 2004
Numerator: Net income	$ 1,935	$ 6,820
Denominator:		
Denominator for basic earnings per share – weighted average shares	26,373	25,543
Effect of dilutive securities:		
Employee and director stock options	1,415	1,807
Denominator for diluted earnings per share – adjusted weighted average shares and assumed conversions	27,788	27,350
Basic earnings per share	$ 0.07	$ 0.27
Diluted earnings per share	$ 0.07	$ 0.25
Options excluded from diluted net earnings per share calculations (1)	69	49

(1) At March 31, 2005 and 2004, options to purchase 69,000 and 49,000 shares, respectively, of Inter-Tel stock were excluded from the calculation of diluted net earnings per share because the exercise price of these options was greater than the average market price of the common shares for the respective fiscal years, and therefore the effect would have been antidilutive.

NOTE C – ACQUISITIONS, TECHNOLOGY INVESTMENTS AND RESTRUCTURING CHARGES

Lake. On February 28, 2005, Inter-Tel Lake Ltd., a wholly owned Irish subsidiary of Inter-Tel Incorporated ("Inter-Tel") executed an agreement for the purchase of 100% of the issued share capital of Lake Communications Limited and certain affiliated entities (collectively, "Lake") for $28.7 million (including capitalized transaction costs of $0.7 million), plus an earn-out of up to $17.6 million based upon certain targets relating to operating results for Lake through the first eighteen months following the closing date of the transaction. The transaction closed out of escrow on March 4, 2005 upon the release from escrow of closing documentation. In total, the company recorded $19.3 million of intangible assets of which $2.6 million was charged to expense in the first quarter of 2005 as in-process research and development costs with the balance being amortized over eight years. Additionally we recorded $6.6 million of goodwill, which is non-amortizable.

Lake, based in Dublin, Ireland, is a provider of converged communications products in the under 40 user market, including EncoreCX® products currently being distributed by Inter-Tel in the United States. Lake

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designs and develops its products for sale through a distribution network of telecom operators and distributors, including Inter-Tel in the United States. Lake outsources its manufacturing to third-party suppliers. For more than a year, Lake has sold certain communication products to the company in the ordinary course of business.

New Sales Offices in 2004. In January, July and October 2004, we acquired certain assets and assumed certain liabilities relating to the customer bases of former dealers in Nashville and Memphis, Tennessee; Greenville, South Carolina; Pittsburgh, Pennsylvania and Las Vegas, Nevada. The total assets acquired and liabilities assumed from these acquisitions were approximately $1.7 million and $0.4 million, respectively. Purchased intangibles and goodwill recorded as a result of the transactions totaled $0.9 million and $2.7 million, respectively. The goodwill is non-amortizable. The balances included in other purchased intangible assets are being amortized over a period of five years from the date of each acquisition.

New Technology Investments in 2004. In October 2004, the Company acquired certain assets and assumed certain liabilities of Converging Technologies, Inc. The acquired assets primarily include Web-based conferencing solutions, notably Linktivity® software. Tangible assets acquired, liabilities assumed and purchased intangibles (all technology related) acquired were $0.5 million, $0.3 million and $3.0 million, respectively. The purchased intangible is being amortized over five years. Also in October 2004, the Company obtained a license of intellectual property from eDial, a division of Alcatel USA Marketing, Inc. for a total price of $1.0 million. The eDial intangible is being amortized over five years.

New Sales Office in 2003. In connection with opening a new sales office in Philadelphia, Pennsylvania during December 2003, we acquired certain assets and assumed certain liabilities relating to a customer base of a former dealer. The total assets acquired and liabilities assumed were approximately $0.6 million and $0.9 million, respectively. Total goodwill and purchased intangibles recorded as a result of the transaction were $0.2 million and $0.1 million, respectively. The goodwill balance is non-amortizable. The balance included in the $0.1 million in other purchased intangible assets is being amortized over a period of five years.

Technology Investment in 2003. In connection with the acquisition of the rights to certain developed technology for a capitalized purchase price of $2.25 million (included in purchased intangible assets) during the year ended December 31, 2003, the Company entered into an arrangement with the selling entity under which the selling entity would perform additional development activities on a cost reimbursement basis through August 15, 2004. Under the terms of the arrangement, the selling entity could also earn bonus payments totaling up to $1,000,000 for meeting certain development milestones. Milestone bonuses totaling $750,000 for the year ended December 31, 2004 were achieved and expensed as research and development costs. Technological feasibility of the underlying technology has not yet been achieved to provide for viable product sales. As of March 31, 2005, the remaining milestone bonus of $250,000 is dependent on future events and is not considered to be probable or reasonably estimable. The following table summarizes details of the expenses in connection with this technology investment recorded during the respective periods:

(In thousands)	Three Months Ended March 31, 2005	Three Months Ended March 31, 2004
Milestone bonus payments	$ —	$ 250
Development activities on a cost reimbursement basis	—	259
Totals	$ —	$ 509

The values for acquired developed technology were determined based on the negotiated prices paid to acquire the technology. Each of our technology acquisitions was made primarily to acquire a specific technology, rather than for the purpose of acquiring an operating company. The technologies acquired have been used to add additional features/applications to our current products, sold separately as new products or obtained primarily for use with our next generation of products.

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The weighted-average amortization period for total purchased intangibles as of March 31, 2005 and December 31, 2004 was approximately 7.45 years and 6.8 years for each period, respectively. The weighted-average amortization period as of March 31, 2005 and December 31, 2004 for developed technology was approximately 7.22 and 7.0 years for each period, respectively, and 7.75 and 5.0 years respectively for customer lists and non-compete agreements.

Each of the acquisitions discussed above were not material business acquisitions either individually or collectively and each has been accounted for using the *purchase method of accounting*. The results of operations of each of these acquisitions have been included in our accompanying consolidated statements of operations from the date of the acquisitions.

Executone Restructuring Charge. During the second quarter of 2000, we recognized a restructuring charge related to acquired Executone operations. We accounted for the restructuring of the Executone operations, including severance and related costs, the shut down and consolidation of the Milford facility and the impairment of assets associated with the restructuring as identified in the table below. Accrued costs associated with this plan were estimates, although the original estimates made for the second quarter of 2000 for reserve balances have not changed significantly through March 31, 2005.

Exit costs associated with the closure of the Milford facility also included liabilities for building, furniture and equipment lease, and other contractual obligations. We were liable for the lease on the Milford buildings through January 2005. We entered into sublease agreements with third parties to sublease portions of the facility and equipment through that date. The reserve activity for lease and other contractual obligations is identified in the table below.

The total restructuring charge from this event totaled $50.9 million. The following table summarizes details of the restructuring charge in connection with the Executone acquisition, including the description of the type and amount of liabilities assumed, and activity in the reserve balances from the date of the charge through March 31, 2005. Activity represents payments made or amounts written off.

Description	Cash/ Non-Cash	Restructuring Charge	Activity Through 2004	2005 Activity	Reserve Balance At 3/31/05
Personnel Costs:					
Severance and termination costs	Cash	$ (1,583)	$ 1,583	$ —	$ —
Other plant closure costs	Cash	(230)	230	—	—
Lease termination and other contractual obligations (net of anticipated recovery):					
Building and equipment leases	Cash	(7,444)	7,436	8	—
Other contractual obligations	Cash	(1,700)	1,700	—	—
Impairment of Assets:					
Inventories	Non-Cash	(3,454)	3,454	—	—
Prepaid inventory and other expenses	Non-Cash	(2,485)	2,485	—	—
Accounts receivable	Non-Cash	(1,685)	1,685	—	—
Fixed assets	Non-Cash	(3,151)	3,034	3	114
Net intangible assets	Non-Cash	(29,184)	29,184	—	—
Total		**$ (50,916)**	**$50,791**	**$ 11**	**$ 114**

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NOTE D — SEGMENT INFORMATION

Inter-Tel follows Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information" ("SFAS 131"). SFAS 131 established standards for reporting information regarding operating segments in annual financial statements and requires selected information for those segments to be presented in interim financial reports issued to stockholders. SFAS 131 also established standards for related disclosures about products and services and geographic areas. Operating segments are identified as components of an enterprise about which separate discrete financial information is available for evaluation by the chief operating decision maker, or decision-making group, in making decisions as to how to allocate resources and assess performance. The Company's chief decision maker, as defined under SFAS 131, is the Chief Executive Officer.

We view our operations as primarily composed of two segments: (1) our principal segment, which includes sales of telephone systems, telecommunications software, hardware and related services, and (2) network services, including resale of local and long distance calling services, voice circuits and data circuits through NetSolutions®, as well as commissions earned by Network Services Agency, our division serving as an agent selling local and network services such as T-1 access, frame relay and other voice and data circuit services on behalf of Regional Bell Operating Companies (RBOCs) and local exchange carriers (collectively, "Network Services"). Sales of these systems, software, related services and Network Services are provided through the Company's direct sales offices and dealer network to business customers in North America, and in parts of Europe, Australia, South Africa and Asia. As a result, financial information disclosed represents substantially all of the financial information related to the Company's two principal operating segments. Results of operations for the resale of local, long distance and network services segment, if the operations were not included as part of the consolidated group, could differ materially, as the operations are integral to the total telephony solution offered by us to our customers.

For the quarters ended March 31, 2005 and 2004, we generated income from business segments as follows:

	Three Months Ended March 31, 2005		
(In thousands, except per share amounts)	Principal Segment	Resale of Local, Long Distance and Network Services	Total
Net sales	$ 92,659	$ 13,048	$105,707
Gross profit	49,262	4,792	54,054
Operating income	1,768	1,746	3,514
Interest and other income	906	41	947
Foreign currency transaction gains	53	—	53
Interest expense	(23)	—	(23)
Net income	$ 786	$ 1,149	$ 1,935
Net income per diluted share (1)	$ 0.03	$ 0.04	$ 0.07
Weighted average diluted shares (1)	27,788	27,788	27,788
Goodwill	$ 24,325	$ 2,135	$ 26,460
Total assets	403,885	7,968	411,853
Depreciation and amortization	3,062	8	3,070

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(In thousands, except per share amounts)	Three Months Ended March 31, 2004 Principal Segment	Resale of Local, Long Distance and Network Services	Total
Net sales	$ 86,049	$ 11,982	$ 98,031
Gross profit	47,174	4,924	52,098
Operating income	8,455	2,159	10,614
Interest and other income	450	56	506
Foreign currency transaction losses	(161)	—	(161)
Interest expense	(45)	(1)	(46)
Net income	$ 5,444	$ 1,376	$ 6,820
Net income per diluted share (1)	$ 0.20	$ 0.05	$ 0.25
Weighted average diluted shares (1)	27,350	27,350	27,350
Goodwill	$ 15726	$ 2,135	$ 17,861
Total assets	348,511	$ 22,153	$370,664
Depreciation and amortization	2,367	14	2,381

(1) Options that are antidilutive because the exercise price was greater than the average market price of the common shares are not included in the computation of diluted earnings per share.

Our revenues are generated predominantly in the United States. Total revenues generated from U.S. customers totaled $99.8 million, or 94.4% of total revenues, and $94.8 million, or 96.7% of total revenues for the three months ended March 31, 2005 and 2004, respectively. Refer to the table below for additional geographical revenue data.

Source of net sales	Quarter Ended March 31, 2005 $	%	Quarter Ended March 31, 2004 $	%
Domestic	99,753	94.4%	94,781	96.7%
Lake Communications	2,590	2.4	—	—
Other International	3,364	3.2	3,250	3.3
Total net sales	105,707	100.0%	98,031	100.0%

In the first three months of 2005 and 2004, revenues from customers located internationally accounted for 5.6% and 3.3% of total revenues, respectively. 2005 revenue percentages from foreign sources primarily increased as a result of our acquisition of Lake in March 2005. Lake is based in Dublin, Ireland with majority of its sales made to the United Kingdom, Australia, other European countries, and South Africa. Other International revenues identified in the table above primarily consist of revenues from Inter-Tel's UK operations, including sales from Swan Solutions. Our UK offices sell predominantly into the United Kingdom and other European countries. All sales made between Inter-Tel divisions are eliminated and are not represented in the above amounts or in the Consolidated Statements of Income.

Our applicable long-lived assets at March 31, 2005, included Property, Plant & Equipment; Goodwill; and Purchased Intangible Assets. The net amount located in the United States was $55.6 million and the amount in foreign countries was $26.6 million at March 31, 2005. At December 31, 2004, the net amount located in the United States was $56.1 million and the amount in foreign countries was $2.6 million.

NOTE E — NET INVESTMENT IN SALES-LEASES

Net investment in sales-leases represents the value of sales-leases presently held under our Total Solution program. We currently sell the rental payments due to us from most of the sales-leases. We maintain reserves against our estimate of potential credit losses for the balance of sales-leases held and for the balance of sold rental payments remaining unbilled. The following table provides detail on the total net balances in sales-leases:

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(In thousands)	March 31, 2005	December 31, 2004
Lease balances included in consolidated accounts receivable, net of allowances of $1,206 in 2005, and $1,177 in 2004	$ 5,348	$ 6,390
Net investment in Sales-Leases:		
Current portion, net of allowances of $861 in 2005, and $866 in 2004	18,160	17,151
Long-term portion, includes residual amounts of $684 in 2005 and, $510 in 2004, net of allowances of $1,960 in 2005, and $1,810 in 2004	35,781	33,877
Total investment in Sales-Leases, net of allowances of $4,027 in 2005, and $3,873 in 2004	59,289	57,418
Sold rental payments remaining unbilled (subject to limited recourse provisions), net of allowances of $12,721 in 2005, and $12,241 in 2004	236,337	229,163
Total balance of sales-leases and sold rental payments remaining unbilled, net of allowances	$295,626	$ 286,581
Total allowances for entire lease portfolio (including limited recourse liabilities)	$ 16,748	$ 16,114

Reserve levels are established based on portfolio size, loss experience, levels of past due accounts and periodic, detailed reviews of the portfolio. Recourse on the sold rental payments is contractually limited to a percentage of the net credit losses in a given annual period as compared to the beginning portfolio balance for a specific portfolio of sold leases. While our recourse is limited, we maintain reserves at a level that we believe is sufficient to cover all anticipated credit losses. The aggregate reserve for uncollectible lease payments and recourse liability represents the reserve for the entire lease portfolio.

These reserves are either netted against consolidated accounts receivable, netted against current or long-term "investment in sales-leases" or included in long-term liabilities for sold rental payments remaining unbilled. Sales of rental payments per period are as follows:

(In thousands)	Three Months Ended March 31, 2005	Year Ended December 31, 2004
Sales of rental payments	$ 28,944	$ 113,172
Sold payments remaining unbilled at end of period	$ 249,058	$ 241,404

Sales of rental payments represent the gross selling price or total present value of the payment stream on the sale of the rental payments to third parties. Sold payments remaining unbilled at the end of the period represent the total balance of leases that is not included in our balance sheet. We do not expect to incur any significant losses in excess of reserves from the recourse provisions related to the sale of rental payments.

During the first quarter of 2005, the Company entered into a "rate-lock" agreement (the "Agreement") with a financial institution in the form of a commitment to sell the cash flow streams for leases with a present value of at least $22.0 million in June 2005 at an interest rate to the financial institution of 6.25 percent and $17.0 million in December 2005 at an interest rate to the financial institution of 6.30 percent. Should interest rates decrease substantially, the Company has the option to pay $500,000 to the financial institution to cancel the commitment for each of the two sales.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This Quarterly Report to Shareholders on Form 10-Q ("10-Q") contains forward-looking statements that involve risks and uncertainties. The statements contained in this 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including without limitation statements regarding our expectations, beliefs, intentions or strategies for the future. All forward-looking statements included in this document are based on information available to us on the date hereof, and we assume no obligation to update any such forward-looking statements. The cautionary statements made in this 10-Q should be read as being applicable to all related forward-looking statements wherever they appear in this document. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors, including those set forth under "Factors That May Affect Future Operating Results" below and elsewhere in this document.

Overview

Inter-Tel (Nasdaq: INTL), Incorporated in 1969, is a single point of contact, full service provider of converged voice and data business communications systems, voice mail systems and networking applications. Our customers include business enterprises, federal, state and local government agencies and non-profit organizations. We market and sell the following products and services:

- Inter-Tel Axxess® and Inter-Tel 5000 Network Communications Solutions converged voice and data business communication systems,
- Lake Communications converged voice and data business communication systems, including those sold in the US under the EncoreCX® brand,
- Integrated voice mail, voice processing and unified messaging systems,
- IP telephony voice and data routers, and e-commerce software,
- managed services, including voice and data network design and traffic provisioning, custom application development, and financial solutions packages (leasing),
- networking applications, including the design and implementation of voice and data networks,
- local and long distance calling services, voice circuits, data circuits and other communications services and peripheral products,
- call accounting software, computer-telephone integration (CTI) applications, and
- maintenance and support services for our products.

We have developed a distribution network of direct sales offices, dealers and value added resellers (VARs), which sell our products to organizations throughout the United States and internationally, primarily targeting small-to-medium enterprises, service organizations and governmental agencies. As of March 31, 2005, we had fifty-nine (59) direct sales offices in the United States and a network of hundreds of dealers and VARs, primarily in the United States, that purchase directly from us. Included in our sales office in Phoenix is the primary location for our national and government accounts division, as well as our local, long distance and network services divisions. Our wholesale distribution center is located in Tempe, Arizona, which is the primary location from which we distribute products to our network of direct sales offices, dealers and VARs in North America. In addition, we maintain a wholesale distribution office in the United Kingdom that supplies Inter-Tel's dealers and distributors throughout the UK and other parts of Europe, and we have dealers in South Africa and Japan. We also maintain research and development and software sales offices in Tucson, Arizona and in the United Kingdom. In March 2005, as a result of the closing of the Lake acquisition identified below, we will also maintain a wholesale distribution office in Dublin, Ireland that supplies Inter-Tel's dealers and distributors in the UK, Ireland, other parts of Europe and

Australia.

On October 14, 2004, Inter-Tel announced the purchase by an operating subsidiary of selected assets and assumption of certain liabilities of Converging Technologies, Inc. and Linktivity, Inc. The acquired assets primarily include Web-based conferencing solutions, notably Linktivity® software. These solutions provide real-time communications and remote control software to enable instantaneous, browser-to-

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browser Web conferencing and help desk support solutions. We expect the acquisition of these selected assets to enable Inter-Tel to continue to expand its Presence Management and Collaboration tools. Linktivity offers its products and services through its international distributors and certified North American resellers. On that same date, Inter-Tel also announced the license of intellectual property from eDial, a division of Alcatel USA Marketing, Inc., and provider of Session Initiation Protocol (SIP) audio conferencing and collaboration solutions for enterprises and service providers. The eDial and Linktivity technologies were selected to complement Inter-Tel's Converged Business Communication systems and to allow Inter-Tel to further enhance its presence management, conferencing and collaboration products.

On February 28, 2005, Inter-Tel Lake Ltd., a wholly owned Irish subsidiary of Inter-Tel, Incorporated ("Inter-Tel") executed an agreement for the purchase of 100% of the issued share capital of Lake Communications Limited and certain affiliated entities (collectively, "Lake") for $28.7 million (including capitalized transaction costs of $0.7 million), plus an earn-out of up to $17.6 million based upon certain targets relating to operating results for Lake through the first eighteen months following the closing date of the transaction. The transaction closed out of escrow on March 4, 2005 upon the release from escrow of closing documentation. Lake, based in Dublin, Ireland, is a provider of converged communications products in the under 40-user market, including EncoreCX® products distributed by Inter-Tel in the United States. Lake designs and develops its products for sale through a distribution network of telecom operators and distributors, including Inter-Tel in the United States. Lake outsources its manufacturing to third-party suppliers. For more than a year, Lake has sold certain communications products to the Company in the ordinary course of its business.

Key performance indicators that we use in order to manage our business and evaluate our financial and operating performance include revenues, costs and gross margins, and cash flows.

Inter-Tel recognizes revenue from the following significant sources of revenue:

- *End-user sales and sales-type leases through our direct sales offices and government and national accounts division.* We recognize revenue from sales of systems and services to end-user customers upon installation of the systems and performance of the services, respectively, allowing for use by our customers of these systems. We defer pre-payments for communications services and recognize these pre-payments as revenue as the communications services are provided. For our sales-type lease accounting, we record the discounted present values of minimum rental payments under sales-type leases as sales, net of provisions for continuing administration and other expenses over the lease period. We record the lease sales at the time of system sale and installation as discussed above for sales to end user customers, and upon receipt of the executed lease documents. The net rental streams are sold to funding sources on a regular basis with the income streams discounted by prevailing like-term rates at the time of sale. Gains or losses resulting from the sale of net rental payments from such leases are also recorded as net sales.

- *Dealer and VAR sales.* For shipments to dealers and other distributors, our revenue is recognized as products are shipped to the dealers or VARs and services are rendered, because the sales process is complete. Title to these products passes when goods are shipped (free-on-board shipping point). However, in connection with our recent Lake acquisition, shipments to one International dealer are initially held by that dealer on a consignment basis. Such Inventory is owned by Inter-Tel and reported on Inter-Tel's books and records until the Inventory is sold to third parties, at which time the revenue is recorded.

- *Resale of long distance.* We recognize revenue from long distance resale services as services are provided.

- *Software Sales.* We recognize revenues from sales of software, such as our new Linktivity products discussed above upon shipment to dealers or end-users.

- *Maintenance and software support.* Maintenance and software support revenue is recognized ratably over the term of the maintenance or support agreement.

Costs and gross margins. Our costs of products sold primarily consist of materials, labor and overhead. Our costs of services performed consist primarily of labor, materials and service overhead. Total costs of goods and services sold increased 12.5%, or $5.7 million, to $51.7 million for the quarter ended March 31, 2005, compared to $45.9 million for the corresponding period in 2004. Our consolidated gross margin percentage was 51.1% in the first quarter of 2005 compared to 53.1% in the first quarter of

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2004. The increase in the dollar amount of the cost of goods sold was primarily attributable to the higher volume of net sales. However, the decrease in gross margin was principally attributable to significant pricing pressures and product discounts, in particular for larger deals, as well as greater than expected sales of lower margin products as a percentage of total sales, and lower than expected sales in our direct sales offices and government and national accounts businesses, which generally offer higher gross margins compared to our other distribution channels and operations. Other factors affecting both the increases in costs of goods sold and reductions in overall gross margin percentage are described in greater detail in "Results of Operations" below.

Sales of systems through our direct sales organization typically generate higher gross margins than sales through our dealers and VARs, primarily because we recognize both the wholesale and retail margins on these sales. Conversely, sales of systems through our dealers and VARs typically generate lower gross margins than sales through our direct sales organization, although direct sales typically require higher levels of selling, general and administrative expenses. In addition, our long distance services and Datanet products typically generate lower gross margins than sales of software and system products. For revenues recognized under sales-leases, we record the costs of systems installed as costs of sales. Our margins may vary from period to period depending upon the representation of various distribution channels, products and software as relative percentages of our total sales. In the event that sales through our direct sales offices increase as a percentage of net sales, our overall gross margin could improve. Conversely, in the event net sales to dealers or sales of long distance services increase as a percentage of net sales, our overall gross margin could decline.

Additionally, our operating results depend upon a variety of factors, including the volume and timing of orders received during a period, general economic conditions and world events impacting businesses, patterns of capital spending by customers, the timing of new product announcements and releases by us and our competitors, pricing pressures, the cost and impact of acquisitions and the availability and cost of products and components from our suppliers. Historically, a substantial portion of our net sales in a given quarter has been recorded in the third month of the quarter, with a concentration of such net sales in the last two weeks of the quarter. There are several factors which attribute to this pattern, including the following:

- Customer leases generally expire at end of the month and commence at the beginning of the month, which naturally leads to end-of-period sales. These factors apply to both end-user and dealer sales.

- Internal sales compensation programs for our sales personnel are linked to revenues and the sales commissions generally increase at accelerated rates as sales volumes increase. Sales performance bonuses are also frequently tied to quarter-end and year-end performance targets, providing incentives to sales personnel to close business before the end of each quarter.

- Some price discounting to our dealer channel occurs during the last month of a quarter or year, and some dealers purchase consistently to take advantage of potential pricing discounts or end-of-quarter promotions. Dealer buying habits have been consistently applied for years.

In addition, we are subject to seasonal variations in our operating results, as net sales for the first and third quarters are frequently less than those experienced during the fourth and second quarters, respectively. Net sales from the first quarter of 2005 followed this historical pattern, as sales declined compared to the fourth quarter of 2004, and we do not anticipate a significant change in the historical trend.

Cash Flows. At March 31, 2005, Inter-Tel's cash and short-term investments totaled $181.1 million. We also maintain a $10 million unsecured, revolving line of credit with BankOne, NA, which is available through June 1, 2006 and ordinarily used to support international letters of credit to suppliers, if necessary. As of March 31, 2005, none of the credit line was used. Historically, our primary source of cash has come from net income plus non-cash charges for depreciation and amortization expenses. We have generated cash from continuing operations in every year since 1986. In 1993, 1995 and 1997, the Company received net proceeds from stock offerings, offset in part by cash expended to repurchase the Company's common stock in these and other periods. In addition, Inter-Tel historically has paid cash for capital expenditures

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relating to property and equipment or acquisitions. Inter-Tel has also received cash proceeds from the exercise of stock options and our Employee Stock Purchase Plan. We believe our working capital and credit facilities, together with cash generated from operations, will be sufficient to develop and expand our business operations, to finance acquisitions of additional resellers of telephony products and other strategic acquisitions or corporate alliances, to fund the special dividend of $1.00 per share to shareholders of record on March 31, 2005, to repurchase shares of the Company's common stock pursuant to a Board approved repurchase program of up to $75 million announced in February 2005, and to provide adequate working capital for the foreseeable future.

Our consolidated net sales for the quarters ended March 31, 2005 and 2004 were $105.7 million and $98.0 million, respectively. The 7.8% increase in revenue in the first quarter of 2005 compared to the first quarter of 2004 was primarily attributable to acquisitions completed in the second half of 2004 and the Lake acquisition in March 2005 (as the sales from these acquired entities were not included in the 2004 first quarter results), as well as slightly higher net sales in our core business. The increase in net sales can also be attributed in part to improved sales in our local, long distance resale and network services division. Net sales in the first quarter of 2005 were negatively impacted, however, by the delayed release of new products, in particular the Inter-Tel 5000 Network Communications Solutions, which were not released until late April 2005, and discounting of new product sales in our direct sales channels. We cannot provide assurance that the recent increase in revenue will continue in the future, as we believe businesses may be reluctant to significantly increase spending on enterprise communications systems in the near future. In addition, we believe uncertainty exists in the marketplace caused by the transition of communication systems from circuit-switch to packet-switch architectures, including voice over Internet Protocol (VoIP) systems, and some buyers may delay making investments in new systems.

We believe that enterprises continue to be concerned about their ability to increase revenues and profitability, in part due to the continued uncertain economic environment and slowdown in the past few years. To maintain or improve profitability, we believe that businesses have attempted to reduce costs and capital spending. We expect continued pressure on our ability to generate or expand sales and it is not clear whether business communications spending will increase in the near term. We cannot predict the nature, timing and extent of future business investments in communications systems and as a result, if and when our net sales will increase.

The markets in which we compete have been characterized by rapid technological changes and increasing customer requirements. We have sought to address these requirements through the development of software enhancements and improvements to existing systems and the introduction of new systems, products, and applications. Inter-Tel's research and development efforts over the last several years have been focused primarily on the development of, and enhancements to, the Inter-Tel 5000 Network Communications Solutions, our Axxess system, including adding new applications, enhancing our IP convergence applications and IP endpoints, developing Unified Communications applications, developing presence management applications, developing Session Initiation Protocol (SIP) applications, and developing speech-recognition and text-to-speech applications. More recently, Inter-Tel's research and development efforts have been focused on the development of converged systems and software, including the Inter-Tel 5000 Network Communications Solutions, Session Initiation Protocol (SIP) interfaces and applications, as well as the development of a new line of multi-protocol SIP IP endpoints. In addition, in October 2004, we acquired selected assets and assumed certain liabilities of Linktivity, which develops Web-based conferencing solutions, notably Linktivity® software, and announced an agreement to license certain intellectual property from eDial. These solutions are designed to provide real-time communications and remote control software to enable instantaneous, browser-to-browser Web conferencing and help desk support solutions. We intend to further develop this technology and integrate the applications and solutions into our product offerings.

We offer our customers a package of lease financing and other services under the name Total Solution. Total Solution provides our customers lease financing, maintenance and support services, fixed price upgrades and other benefits. We finance this program through the periodic resale of lease rental streams to financial institutions. Refer to Note E of Notes to Condensed Consolidated Financial Statements for additional information regarding our program.

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Results of Operations

The following table sets forth certain statement of operations data expressed as a percentage of net sales for the periods indicated:

	Three Months Ended March 31, 2005	2004
NET SALES		
Telecommunications systems, software and related	87.7%	88.5%
Resale of local, long distance and network services	12.3	11.5
TOTAL NET SALES	100.0	100.0
COST OF SALES		
Telecommunications systems, software and related	41.1	39.7
Resale of local, long distance and network services	7.8	7.2
TOTAL COST OF SALES	48.9	46.9
GROSS PROFIT	51.1	53.1
Research and development	8.0	6.2
Selling, general and administrative	36.6	35.7
Amortization of intangibles	0.7	0.5
Write-off of in-process research and development costs	2.5	—
OPERATING INCOME	3.3	10.8
Interest and other income	0.9	0.5
Foreign currency transaction gains (losses)	0.1	(0.2)
Interest expense	(0.0)	(0.0)
INCOME BEFORE INCOME TAXES	4.2	11.1
INCOME TAXES	2.4	4.2
NET INCOME	1.8%	7.0%

Net Sales. Net sales increased 7.8%, or $7.7 million, to $105.7 million in the first quarter of 2005, from $98.0 million in the first quarter of 2004. Excluding the Lake acquisition in first quarter of 2005, non-GAAP net sales increased 5.2% or $5.1 million compared to net sales for the corresponding prior year period. Sales from our direct sales offices (including revenues from lease financing), increased 5.1%, or $2.8 million, in the first quarter of 2005 compared to the corresponding period in 2004. Sales attributable to our dealer network increased by 1.8%, or $0.4 million, in the first quarter of 2005, compared to the corresponding period in 2004. Sales from our local and long distance resale and network services division increased by 8.9%, or $1.1 million, in the first quarter of 2005, compared to the corresponding period in 2004. Sales from our DataNet division increased 25.3%, or $0.7 million, in the first quarter of 2005, compared to the corresponding period in 2004. International revenues excluding the Lake acquisition increased by 3.5%, or $0.1 million, in the first quarter of 2005, compared to the corresponding period in 2004. Lake sales totaled $2.6 million in the first quarter of 2005. Overall, sales attributable to our government and national accounts division remained relatively unchanged in first quarter of 2005 compared to the corresponding period in 2004.

The increase in net sales for the first quarter of 2005 compared to the corresponding period in 2004 from our direct sales offices, dealer channel, and international operations were primarily attributable to acquisitions completed in the second half of 2004 and the Lake acquisition in March 2005, offset in part by continued competitive pricing pressures and some delayed buying decisions and heavy discounting during the quarter in our direct sales offices. We believe that the announcement of the E-Rate settlement also resulted in some deferred or lost sales. The increases in net sales were also a result of higher volumes of systems sold. In some instances, prices of various telecommunications systems decreased, and discounts or other promotions were offered to customers to generate sales in both our direct and indirect channels.

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Recurring revenues from existing customers increased on a percentage basis and dollar volume relative to sales to new customers in our direct sales channel during the first quarter of 2005.

Sales from our local, long distance resale and network services divisions (NetSolutions® and Network Services Agency) and our DataNet division increased in the first quarter of 2005 as compared to the corresponding period in 2004. Net sales increased by 6.9%, or $0.8 million, to $12.0 million in the first quarter of 2005, compared to $11.2 million in the corresponding period in 2004 for NetSolutions®, despite downward pricing pressure and significant competition. Increased sales volume has allowed NetSolutions ® to offer more competitive pricing, which improved sales to our existing customer base. Sales increased in DataNet primarily due to additional sales to a few customers. Net sales from Network Services Agency, a commission-based sales unit within the local, long distance resale and network services division acting as an agent to sell services for selected RBOC's and CLEC's, increased $0.3 million, to $1.0 million in the quarter ended March 31, 2005 compared to $0.7 million in the corresponding period in 2004. See Note D of Notes to Condensed Consolidated Financial Statements for additional segment reporting information.

Gross Profit. Gross profit for the first quarter of 2005 increased 3.8% to $54.1 million, or 51.1% of net sales, from $52.1 million, or 53.1% of net sales, in the first quarter of 2004. The increase in gross profit dollars in the first quarter of 2005 resulted primarily from a higher volume of consolidated net sales. The decrease in gross profit as a percentage of sales was primarily a result of industry pricing pressures, leading to discounting and special promotions on telephone system sales. Increased sales from the resale of local and long distance services also had the effect of decreasing the consolidated gross profit percentage, as these revenues typically generate lower gross margins. Higher relative recurring revenues from existing customers partially offset the decreases in gross profit percentage.

During the first quarter of 2005, recurring revenue dollars from existing customers in our direct sales, DataNet and national and government accounts channels increased from these same channels relative to the first quarter of 2004. As a percentage of sales, recurring revenues increased in the direct sales and DataNet channels and remained relatively constant for the national and government accounts channel. Existing customers accounted for a significant portion of our net sales from maintenance and other services, software additions and/or upgrades, and other peripheral products such as video conferencing, call logging solutions, wireless endpoints, power protection, wired and wireless headsets, audio conferencing units and networking products during the first quarter of 2005. Our business communications platforms allow for system migration without the complete replacement of hardware, enabling us to offer enhancements and new solutions through software-only upgrades to our existing customers. Consequently, our gross margins are generally higher with recurring revenues because we incur less materials costs relative to new installations.

Sales from NetSolutions® increased by 6.9%, or $0.8 million, in the first quarter of 2005 as compared to the first quarter of 2004. Gross margins are generally lower in this division than our consolidated margins. Sales from Network Services Agency, increased 40.0%, or $0.3 million, for the first quarter of 2005 compared to the corresponding period in 2004. This division generally receives commissions on network services we sell as an agent for Regional Bell Operating Companies. Sales from this division carry little to no equipment costs and generated margins of 86.2% during the first quarter of 2005. Accordingly, the increase in sales from this division offset in part our decrease in consolidated gross profit percentage.

We cannot accurately predict future consolidated gross margins because of period-to-period variations in a number of factors, including among others, competitive pricing pressures, sales of systems, software and services through different distribution channels, supplier and agency agreements, and the mix of systems, software and services we sell.

Research and Development. Research and development expenses for the first quarter of 2005 increased 40.1% to $8.5 million, or 8.0% of net sales, from $6.0 million, or 6.2% of net sales, for the first quarter of 2004. Included in research and development expenses in both the first quarter of 2005 and the first quarter of 2004 was amortization of patents totaling $55,000 in each period. The increases in research and development expenses for the first quarter ended March 31, 2005 were primarily attributable to the increased engineering headcount and third-party outsourcing of selected development costs in connection with our efforts to accelerate development of new products and software, as well as additional research and development costs associated with our acquired

Lake and Linktivity operations. The increases were also

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attributable to increased research and development spending related to our development of convergence applications and new SIP and IP endpoint technology. In the first quarter ended March 31, 2005, research and development expenses were directed principally toward the continued development of converged systems and software, including the Inter-Tel 5000, unified messaging and voice processing software, speech recognition and text-to-speech applications, call center applications, unified communications applications, IP endpoint development, and certain CTI and IVR applications and SIP applications. Through 2005, we expect that research and development expenses will increase in absolute dollars and as a percentage of net sales relative to 2004 due primarily to research and development costs from the acquired Lake and Linktivity operations, and our efforts to continue to develop and enhance existing and new technologies and products.

Selling, general and administrative. In the first quarter of 2005, selling, general and administrative expenses increased 10.6% to $38.7 million, or 36.6% of net sales, from $35.0 million, or 35.7% of net sales, in the first quarter of 2004. The increases in absolute dollars and as a percentage of net sales were primarily due to higher expenses associated with the increases in consolidated net sales in 2005 compared to 2004. Expenses also increased as a result of the acquisition of new sales offices in South Carolina, Las Vegas, Pittsburgh and Tucson (Linktivity) during the second half of 2004, as well as the Lake operations in Dublin, Ireland. In addition, higher net sales led to increased selling expenses and commission costs in the first quarter of 2005 relative to such costs for the corresponding periods in 2004. In the first quarter of 2005, selling, general and administrative expenses also increased as a result of higher depreciation expense, offset in part by lower bad debts relative to 2004. We expect that for the foreseeable future selling, general and administrative expenses may vary in absolute dollars and as a percentage of net sales.

Amortization of purchased intangible assets. We adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142") effective in the beginning of fiscal 2002. In accordance with SFAS 142, we ceased amortizing goodwill. We are required to perform goodwill impairment tests on an annual basis and between annual tests in certain circumstances. As of March 31, 2005, no impairment of goodwill has been recognized in 2005. We face the risk that future goodwill impairment tests may result in charges to earnings.

Amortization of purchased intangible assets included in operating expenses was $762,000 in the first quarter of 2005, compared to $445,000 in the first quarter of 2004. In addition, $55,000 of amortization was included in research and development expenses for the first quarter of 2005 and the first quarter of 2004. The increase in the amortization of purchased intangible assets for the first quarter 2005 compared to the same period in 2004 was primarily related to the additional amortization from recent acquisitions, primarily the Lake and Linktivity acquisitions. For additional information regarding purchased intangible assets, see Note C "Acquisitions, Technology Investments and Restructuring Charges" to the Condensed Consolidated Financial Statements.

Write-off of in-process research and development (IPRD) costs. During the first quarter of 2005, Inter-Tel completed the acquisition of Lake (see NOTE C). The aggregate purchase price of the Lake acquisition was allocated to the fair value of the assets and liabilities acquired, of which $2.6 million, or $0.09 per diluted share, was written-off as purchased IPRD. Without this write-off, the Company would have reported non-GAAP net income of $4.5 million ($0.16 per diluted share) for the three months ended March 31, 2005 instead of the $1.9 million ($0.07 per diluted share) reported.

Interest and Other Income. Interest and other income in 2005 and 2004 consisted primarily of interest income and foreign currency transaction gains or losses. The net increase in interest and other income of $441,000 in the first quarter of 2005 compared to the corresponding period in 2004 was due primarily to higher levels of invested funds, as well as higher interest rates. Net foreign currency transaction gains in the first three months of 2005 were $53,000 compared to losses of $161,000 in the first three months of 2004. Interest expense was nominal in both periods, totaling $23,000 in the first three months of 2005 compared to $46,000 in the first three months of 2004.

Income Taxes. Inter-Tel's income tax rate for the first quarter of 2005 was 56.9% compared to 37.5% for the first quarter of 2004. The increase in the rate was primarily attributable to the write-off of in-process research and development costs in connection with our Lake acquisition, because these costs are

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not deductible for tax purposes. Inter-Tel currently expects the full-year 2005 tax rate to be 37.8%, subject to prospective changes in the tax laws or other factors. Excluding the acquisition of Lake, the non-GAAP, or pro forma, full-year rate for 2005 is currently projected to be 36%, a decrease compared to 2004. This pro forma decrease compared to 2004 is expected due to several factors, including the differences between the projected 2005 and 2004 results, in particular higher projected 2005 tax-exempt interest and higher utilization of 2005 research and development credits. The 2005 rate is subject to change based on the projected results of operations, including the Lake acquisition and other factors identified above.

Net Income. Net income for the first quarter of 2005 was $1.9 million ($0.07 per diluted share), a decrease of 71.6% compared to net income of $6.8 million ($0.25 per diluted share) in the first quarter of 2004.

The decrease in net income for the first quarter and of 2005 compared to the corresponding period in 2004 was primarily attributable to the write-off of IPRD costs in connection with the Lake acquisition, lower gross margins as a result of competitive pressures and product discounting, higher research and development expenses, higher selling, general and administrative expenses, and higher amortization expenses, offset in part by operating profits from higher relative net sales. Excluding the write-off of IPRD, the Company would have reported net income of $4.5 million ($0.16 per diluted share) for the three months ended March 31, 2005. Additional information regarding other items is described in further detail above.

Inflation/Currency Fluctuation

Inflation and currency fluctuations have not previously had a material impact on Inter-Tel's operations. Inter-Tel's International procurement agreements have traditionally been denominated in U.S. currency. Moreover, a significant amount of contract manufacturing has been or may be moved to alternative sources. The expansion of international operations in the United Kingdom and Europe and increased sales, if any, in Ireland, Europe and Australia as a result of the 2005 Lake acquisition could result in higher international sales as a percentage of total revenues; however, international revenues do not currently represent a significant portion of our total revenues.

Liquidity and Capital Resources

(In thousands)	Three Months Ended March 31, 2005	Three Months Ended March 31, 2004
Net cash (used in) provided by operating activities	$ (2,407)	$ 15,920
Net cash (used in) provided by investing activities	(28,463)	1,183
Net cash provided by financing activities	3,900	1,698
Effect of exchange rate changes	464	292
Increase (decrease) in cash and equivalents	(26,506)	19,093
Cash and equivalents at beginning of period	152,330	115,197
Cash and equivalents at end of period	$125,824	$134,290

At March 31, 2005, cash and equivalents and short-term investments totaled $181.1 million, a decrease of approximately $23.8 million from the balance at December 31, 2004. In addition, long-term investments in marketable debt securities totaled $5.9 million at March 31, 2005, a decrease of $4.0 million from the balance at December 31, 2004. We maintain a $10 million unsecured, revolving line of credit with JPMorgan Chase Bank, N.A. (formerly BankOne, NA) that is available through June 1, 2006. Under the credit facility, we have the option to borrow at a prime rate or adjusted LIBOR interest rate. Historically, we have used the credit facility primarily to support international letters of credit to suppliers. As of March 31, 2005, none of the credit line was used. The remaining cash balances may be used for acquisitions, strategic alliances, working capital, dividends and general corporate purposes.

Net cash used in operating activities totaled $2.4 million for the three months ended March 31, 2005, compared to $15.9 million provided by operating activities for the corresponding period in 2004. Cash used in operating activities in the first three months of 2005 was primarily the result of an $11.9 million change in operating assets and liabilities (including E-Rate of $8.5 million), offset by cash generated from profitable operations, adding back non-cash items such as depreciation, amortization, purchased in process research

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and development and provisions for losses. The net cash provided by operating activities in the first three months of 2004 was primarily the result of cash generated from profitable operations as in 2005; however, the 2004 period did not include any purchased in-process research and development costs. In addition, the first three months of 2004 reflected cash generated by an increase in deferred income taxes of $4.9 million and a change of operating assets and liabilities of $1.1 million. The cash used in the change in operating assets and liabilities in the first three months of 2005 was primarily due to the payment of the E-rate settlement costs totaling $8.5 million (described below), as well as an increase in inventories, investment in sales-leases and income tax receivables, offset in part by increases in accounts payable and a decrease in accounts receivable. The $1.1 million cash provided by the change in operating assets and liabilities in the first three months of 2004 was primarily a result of a decrease in the income tax receivable and accounts receivable, offset in part by an increase in inventories and a decrease in accrued expenses. We expect to expand sales through our direct sales offices and dealer networks, which is expected to require the expenditure of working capital for increased accounts receivable, inventories and net investment in sales-lease.

Net cash used in investing activities totaled $28.5 million for the quarter ended March 31, 2005, compared to cash provided by investing activities of $1.2 million for the quarter ended March 31, 2004. The change from 2004 to 2005 was primarily a result of $27.6 million in cash used for acquisitions in the first quarter of 2005. There was no cash used for acquisitions in the first quarter of 2004. Net cash generated by maturities and sales of short-term investments during the first three months of 2005 was $11.6 million, offset by net cash used in the purchase of short-term investments of $10.3 million. Net cash was generated by maturities and sales of short-term investments of $22.4 million in the first quarter of 2004, offset by cash used in the purchase of long-term and short-term investments of $20.0 million. Net cash of $2.2 million was used to acquire additional property, plant and equipment during the first quarter of 2005 compared to $1.2 million for the corresponding period in 2004.

Net cash provided by financing activities totaled $3.9 million for the quarter ended March 31, 2005, compared to $1.7 million for the corresponding period in 2004. Net cash used for cash dividends totaled $1.8 million in the first quarter of 2005 compared to $1.5 million in the same period for 2004. Net cash provided by proceeds from the exercise of stock options totaled $5.7 million in the first quarter of 2005 compared to $3.2 million in the same period for 2004. During the first quarter of 2005 we reissued treasury shares through stock option exercises and issuances, with the proceeds received totaling less than the cost basis of the treasury stock reissued. Accordingly, the difference was recorded as a decrease to retained earnings of $1.3 million. During the first quarter of 2004 we reissued treasury shares through stock option exercises and issuances, with the proceeds received totaling more than the cost basis of the treasury stock reissued. Accordingly, the difference was recorded as an increase to retained earnings of $0.5 million.

We offer to our customers lease financing and other services, including our Total Solution (formerly Totalease) program, through our Inter-Tel Leasing, Inc. subsidiary. We fund our Total Solution program in part through the sale to financial institutions of rental payment streams under the leases. Sold lease rentals totaling $249.1 million and $241.4 million remained unbilled at March 31, 2005 and December 31, 2004, respectively. We are obligated to repurchase such income streams in the event of defaults by lease customers and, accordingly, maintain reserves based on loss experience and past due accounts. Although, to date, we have been able to resell the rental streams from leases under the Total Solution program profitably and on a substantially current basis, the timing and profitability of lease resales could impact our business and operating results, particularly in an environment of fluctuating interest rates and economic uncertainty. If we are required to repurchase rental streams and realize losses thereon in amounts exceeding our reserves, our operating results will be adversely affected.

During the first quarter of 2005, the Company entered into a "rate-lock" agreement (the "Agreement") with a financial institution in the form of a commitment to sell the cash flow streams for leases with a present value of at least $22.0 million in June 2005 at an interest rate to the financial institution of 6.25 percent and $17.0 million in December 2005 at an interest rate to the financial institution of 6.30 percent. Should interest rates decrease substantially, the Company has the option to pay $500,000 to the financial institution to cancel the commitment for each of the two sales.

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On January 5, 2005, the Company received court approval of a civil settlement agreement (the "Civil Settlement") and a criminal plea agreement (the "Plea Agreement") with the United States of America, each dated as of December 8, 2004 and disclosed on that same date. The court approval of the Civil Settlement and Plea Agreement resolves the investigation of the Department of Justice into the participation of Inter-Tel Technologies, Inc., the Company's wholly-owned subsidiary ("Technologies") in a federally administered "E-Rate program" to connect schools and libraries to the Internet.In connection with the Civil Settlement, Technologies agreed to pay a penalty of $6,740,450 and forego the collection of certain accounts receivable of $259,540 related to Technologies' participation in the E-Rate program.In connection with the Plea Agreement, Technologies entered guilty pleas to charges of mail fraud and an antitrust violation. Under the Plea Agreement, Technologies agreed to pay a fine of $1,721,000 and observe a three-year probationary period, which will, among other things, require Technologies to implement a comprehensive corporate compliance program. The penalties and fines described above were paid in the first quarter of 2005.

In addition, on January 21, 2005, Inter-Tel Technologies received notification from the Federal Communications Commission that Technologies was temporarily suspended from participation in the E-Rate program pending a proposed debarment. Technologies has contested the scope and length of the proposed debarment from the E-Rate program, but there can be no assurance that Technologies will be successful in this regard. Revenues in 2004 relating to Technologies' participation in the E-Rate program were not significant.

The existence and disclosure of the Civil Settlement, Plea Agreement and FCC Notice may have already caused competitive harm to Inter-Tel, and these matters may further harm Inter-Tel's business.

We believe our working capital and credit facilities, together with cash generated from operations, will be sufficient to develop and expand our business operations, to finance acquisitions of additional resellers of telephony products and other strategic acquisitions or corporate alliances, to fund the special dividend of $1.00 per share to shareholders of record on March 31, 2005, to repurchase shares of the Company's common stock pursuant to the Board-approved $75 million repurchase program announced in February 2005, and to provide adequate working capital for the foreseeable future. However, to the extent additional funds are required in the future to address working capital needs and to provide funding for capital expenditures, expansion of the business or additional acquisitions, we will seek additional financing. There can be no assurance additional financing will be available when required or on acceptable terms.

Off-Balance Sheet Arrangements

As part of our ongoing business, we do not participate in transactions that involve unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, which have been established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. However, we offer to our customers lease financing and other services through our Inter-Tel Leasing, Inc. subsidiary. We fund our Total Solution program in part through the sale to financial institutions of rental payment streams under the leases. Such financial institutions have the option to require us to repurchase such income streams, subject to limitations, in the event of defaults by lease customers and, accordingly, we maintain reserves based on loss experience and past due accounts. For more information regarding our lease portfolio and financing, please see "Liquidity and Capital Resources" and Note E of Notes to Condensed Consolidated Financial Statements.

Critical Accounting Policies and Estimates

The methods, estimates and judgments we use in applying our most critical accounting policies have a significant impact on the results we report in our condensed consolidated financial statements. We evaluate our estimates and judgments on an on-going basis. We base our estimates on historical experience and on assumptions that we believe to be reasonable under the circumstances. Our experience and assumptions form the basis for our judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Actual results may vary from what we anticipate and different assumptions or estimates about the future could change our reported results. We believe the following accounting policies are the most critical to us, in that they are important to the portrayal of our

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financial statements and they require our most difficult, subjective or complex judgments in the preparation of our condensed consolidated financial statements:

Revenue Recognition. In December 2003, the Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin No. 104 (SAB 104), "Revenue Recognition." The Company applies the provisions of SAB 104 to all revenue transactions. SAB 104 supercedes SAB 101, "Revenue Recognition in Financial Statements." The primary purpose of SAB 104 is to rescind accounting guidance contained in SAB 101 related to multiple element revenue arrangements, superceded as a result of the issuance of EITF 00-21. Additionally, SAB 104 rescinded the SEC's Revenue Recognition in Financial Statements Frequently Asked Questions and Answers ("the FAQ") issued with SAB 101 that had been codified in SEC Topic 13, Revenue Recognition. Selected portions of the FAQ have been incorporated into SAB 104. While the wording of SAB 104 has changed to reflect the issuance of EITF 00-21, the revenue recognition principles of SAB 101 remain largely unchanged by the issuance of SAB 104. The issuance of SAB 104 did not have a material impact on the Company's financial position, results of operations or cash flows.

End-user sales through our direct sales offices and government and national accounts division. Revenue is recognized when all four of the following criteria are met: (i) persuasive evidence that arrangement exists; (ii) delivery of the products and/or services has occurred; (iii) the selling price is both fixed and determinable and; (iv) collectibility is reasonably probable. Revenue derived from sales of systems and services to end-user customers is recognized upon primary installation of the systems and performance of the services, respectively, allowing for use by our customers of these systems. Pre-payments for communications services are deferred and recognized as revenue as the communications services are provided. We do not generally allow sales returns either by the terms of our contracts or in practice, except for returns related to warranty provisions.

Dealer and VAR sales. For shipments to dealers and other distributors, our revenues are recorded as products are shipped and services are rendered, when the sales process is complete. These shipments are primarily to third-party dealers and distributors, and title passes when goods are shipped (free-on-board shipping point). However, in connection with our recent Lake acquisition, shipments to one international dealer are initially held by that dealer on a consignment basis. Such inventory is owned by Inter-Tel and reported on Inter-Tel's books and records until the inventory is sold to third parties, at which time the revenue is recorded. We do not generally allow sales returns either by the terms of our contracts or in practice, except for returns related to warranty provisions. We provide a number of incentives, promotions and awards to certain dealers and other distributors. These incentives primarily represent discounts (which are recognized as a reduction of sales), advertising allowances and awards (which are recognized as marketing expense) and management assistance (which is expensed as incurred).

Resale of long distance. We recognize revenue from long distance resale services as services are provided.

Maintenance revenues. We recognize maintenance revenue ratably over the term of applicable maintenance agreements.

Sales-Leases. For our sales-type lease accounting, we follow the guidance provided by FASB Statement No. 13, Accounting for Leases and FASB Statement No. 140, Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities – A Replacement of FASB Statement No. 125. We record the discounted present values of minimum rental payments under sales-type leases as sales, net of provisions for continuing administration and other expenses over the lease period. We record the lease sales at the time of system sale and installation pursuant to Staff Accounting Bulletin No. 104, as discussed above for sales to end user customers. The costs of systems installed under these sales-leases are recorded as costs of sales. The net rental streams are sold to funding sources on a regular basis with the income streams discounted by prevailing like-term rates at the time of sale. Gains or losses resulting from the sale of net rental payments from such leases are recorded as net sales. We establish and maintain reserves against potential recourse following the resales based upon historical loss experience, past due accounts and specific account analysis. The allowance for uncollectible minimum lease payments and recourse liability at the end of the year represents reserves against the entire lease portfolio. Management reviews the adequacy of the allowance on a regular basis and adjusts the allowance as required. These reserves are either netted in the accounts receivable, current and long-term components

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of "Net investments in Sales-Leases" on the balance sheet, or included in long-term liabilities on our balance sheet for off-balance sheet leases.

Historically, our reserves have been adequate to cover write-offs. Our total reserve for losses related to the entire lease portfolio, including amounts classified as accounts receivable in our balance sheet, increased slightly from 5.32% at December 31, 2004 to 5.36% at March 31, 2005, primarily as a result of reviews of our write-off experience and accounts receivable agings. Should the financial condition of our customers deteriorate in the future, additional reserves in amounts that could be material to the financial statements could be required.

Goodwill and Other Intangible Assets. On January 1, 2002, Inter-Tel adopted SFAS No. 141, *Business Combinations*, and SFAS No. 142, *Goodwill and Other Intangible Assets.* Purchase prices of acquired businesses that are accounted for as purchases have been allocated to the assets and liabilities acquired based on the estimated fair values on the respective acquisition dates. Based on these values, the excess purchase prices over the fair value of the net assets acquired were allocated to goodwill.

Prior to January 1, 2002, Inter-Tel amortized goodwill over the useful life of the underlying asset, not to exceed 40 years. On January 1, 2002, Inter-Tel began accounting for goodwill under the provisions of SFAS Nos. 141 and 142 and discontinued the amortization of goodwill after January 1, 2002. As of March 31, 2005, Inter-Tel had gross goodwill of $31.5 million and accumulated amortization of $5 million. Inter-Tel completed one acquisition through March 31, 2005 and five in 2004 and has not recorded any amortization for these acquisitions on amounts allocated to goodwill in accordance with SFAS No. 141.

The Company performs an annual impairment test on Goodwill using the two-step process prescribed in SFAS No. 142. The first step is a screen for potential impairment, while the second step measures the amount of the impairment, if any. In addition, the Company will perform impairment tests during any reporting period in which events or changes in circumstances indicate that an impairment may have incurred. Inter-Tel performed the first step of the required impairment tests for goodwill as of December 31, 2004 and determined that goodwill is not impaired and it is not necessary to record any impairment losses related to goodwill. At March 31, 2005 and December 31, 2004, $24.4 million and $17.8 million, respectively, of the Company's goodwill, net of amortization, relates to the Company's principal segment and $2.1 million relates to the Resale of Local, Long Distance and Network Services segment. There is only one reporting unit (i.e., one component) as defined in paragraph 30 of SFAS 142 within each of the Company's two operating segments as defined in paragraph 10 of SFAS 131. Therefore the reporting units are identical to the segments. Fair value has been determined for each segment in order to determine the recoverability of the recorded goodwill. At December 31, 2004, the Company primarily considered an allocated portion of the market capitalization for the entire Company using average common stock prices in determining that no impairment had occurred. This allocated market capitalization value far exceeded the net carrying value of the goodwill included in the financial statements. Therefore, the second step for potential impairment was unnecessary.

The Company evaluates the remaining useful lives of its purchased intangible assets, all of which are subject to amortization, each reporting period. Any changes to estimated remaining lives prospectively effect the remaining period of amortization. In addition, the purchased intangible assets are reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. A loss would be recognized for any excess of the carrying amount over the estimated fair value. As of March 31, 2005, Inter-Tel had gross purchased intangible assets of $35.8 million and accumulated amortization of $8.9 million.

At March 31, 2005 and December 31, 2004, goodwill, net of accumulated amortization, totaled $26.5 million and $19.9 million, respectively. Other acquisition-related intangibles, net of accumulated amortization, totaled $26.9 million at March 31, 2005 and $11.0 million at December 31, 2004. Accumulated amortization through March 31, 2005 was $13.9 million, including $5.0 million of accumulated amortization attributable to goodwill and $8.9 million of accumulated amortization of other acquisition-related intangibles. Accumulated amortization through December 31, 2004 was $13.1 million, including $5.0 million of accumulated amortization attributable to goodwill and $8.1 million of accumulated amortization of other acquisition-related intangibles. Other acquisition-related intangibles, comprised primarily of developed technology (5-10 year lives), customer lists (5-8 year lives) and non-competition

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agreements (2-8 year lives), are amortized on a straight-line basis. The useful lives for developed technology are based on the remaining lives of patents acquired or the estimated useful life of the technology, whichever is shorter. The useful lives of the customer lists are based on the expected period of value for such lists. The useful lives for non-competition agreements are based on the contractual terms of the agreements.

Allowance for Doubtful Accounts. We maintain allowances for doubtful accounts for estimated losses resulting from the inability of our customers to make required payments. Additional reserves or allowances for doubtful accounts are recorded for our sales-type leases, discussed above in "Sales-Leases." We establish and maintain reserves against estimated losses based upon historical loss experience, past due accounts and specific account analysis. Management reviews the level of the allowances for doubtful accounts on a regular basis and adjusts the level of the allowances as needed. In evaluating our allowance we consider accounts in excess of 60 days old as well as other risks in the more current portions of the accounts included. At March 31, 2005, our allowance for doubtful accounts for accounts receivable were \$9.4 million of our \$52.4 million in gross accounts receivable. If the financial condition of our customers or channel partners were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Inventories. We value our inventories at the lower of cost (principally on a standard cost basis, which approximates the first-in, first-out (FIFO) method) or market. Significant management judgment is required to determine the reserve for obsolete or excess inventory and we make our assessment primarily on a significant product-by-product basis for the immediately preceding twelve-month period, adjusted for expected changes in projected sales or marketing demand. Inventory on hand may exceed future demand either because the product is outdated or obsolete, or because the amount on hand is more than can be used to meet estimated future needs. We consider criteria such as customer demand, product life cycles, changing technologies, slow moving inventory and market conditions and we reserve for our excess and possible obsolete inventory. Historically, sales of scrap have not been material and have not affected our profit margins. At March 31, 2005, our inventory reserves were \$7.0 million of our \$26.3 million gross inventories. If actual customer demand, product life cycles, changing technologies and market conditions are less favorable than those projected by management, additional inventory reserves may be required in the future.

Contingencies. We are a party to various claims and litigation in the normal course of business. Management's current estimated range of liability related to various claims and pending litigation is based on claims for which management can estimate the amount and range of loss, or can estimate a minimum amount of a loss. Because of the uncertainties related to both the amount and range of loss on the remaining pending claims and litigation, management is unable to make a reasonable estimate of the liability that could result from an unfavorable outcome. As additional information becomes available, we will assess the potential liability related to our claims and pending litigation, revise our estimates and accrue for any losses to the extent that they are probable and the amount is estimable. Such revisions in our estimates of the potential liability could materially impact our results of operations and financial position.

FACTORS THAT MAY AFFECT FUTURE OPERATING RESULTS

This Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. Actual results could differ materially from those projected in the forward-looking statements as a result of many risk factors including, without limitation, those set forth under "Factors That May Affect Future Results Of Operations" below. In evaluating Inter-Tel's business, shareholders and prospective investors should consider carefully the following factors in addition to the other information set forth in this document.

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Risks Related to Our Business

Our operating results have historically depended on a number of factors, and these factors may cause our operating results to fluctuate in the future.

Our quarterly operating results have historically depended on, and may fluctuate in the future as a result of, many factors including:

- volume and timing of orders received during the quarter;
- gross margin fluctuations associated with the mix of products sold;
- the mix of distribution channels;
- general economic conditions and the condition of the markets our business addresses;
- patterns of capital spending by customers;
- the timing of new product announcements and releases by us and our competitors and other competitive factors;
- pricing pressures;
- the cost and effect of acquisitions;
- the availability and cost of products and components from our suppliers, including shipping and manufacturing problems associated with subcontracted vendors;
- the impact of the E-Rate settlement and possible FCC debarment, which could effect both our government business and our commercial business;
- the potential impact of new accounting pronouncements_such as FAS 123R;
- national and regional weather patterns; and
- threats of or outbreaks of war, hostilities, terrorist acts or other civil disturbances.

In addition, we have historically operated with a relatively small backlog, with sales and operating results in any quarter depending principally on orders booked and shipped in that quarter. In the past, we have recorded a substantial portion of our net sales for a given quarter in the third month of that quarter, with a concentration of such net sales in the last two weeks of the quarter. Market demand for investment in capital equipment such as business communications systems and associated call processing and voice processing software applications depends largely on general economic conditions and can vary significantly as a result of changing conditions in the economy as a whole, as well as heightened competitive pressures. We cannot assure you that we can continue to be successful operating with a small backlog or whether historical backlog trends will continue in the future.

Our expense levels are based in part on expectations of future sales and, if sales levels do not meet expectations, our operating results could be harmed. In addition, because sales of business communications systems through our dealers typically produce lower gross margins than sales through our direct sales organization, operating results have varied, and will continue to vary based upon the mix of sales through direct and indirect channels. In addition, in the recent past we have derived a significant part of our revenue from recurring revenue streams, which typically produce higher gross margins. If we do not maintain recurring revenue streams at current or historic levels, our operating results would suffer unless we significantly increased sales to new customers. Moreover, particularly in an environment of fluctuating interest rates, the timing and profitability of lease resales from quarter to quarter could impact operating results. Long distance and DataNet sales, which typically carry lower gross margins than our core business, have grown in recent periods at a faster rate than our overall net sales, although gross margins may fluctuate in these divisions from period to period. Consolidated gross margins could be harmed if long distance calling services continue to increase as a percentage of net sales or if gross margins from this division decline. We also experience seasonal fluctuations in our operating results, as net sales for the first quarter is frequently less than the fourth quarter, and net sales for the third quarter is frequently less than the second quarter. As a result of these and other factors, we have historically experienced, and could continue to experience in the future, fluctuations in net sales and operating results on a quarterly basis.

Our market is subject to rapid technological change and to compete successfully, we must continually introduce new and enhanced products and services that achieve broad market acceptance.

The market for our products and services is characterized by rapid technological change, evolving industry standards and vigorous customer demand for new products, applications and services. To compete successfully, we must continually enhance our existing telecommunications products, related

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software and customer services, and develop new technologies and applications in a timely and cost-effective manner. If we fail to introduce new products and services that achieve broad market acceptance and on a timely basis, or if we do not adapt our existing products and services to customer demands or evolving industry standards, our business could be significantly harmed. Problems and delays associated with new product development have in the past contributed to lost sales. In addition, current competitors or new market entrants may offer products, applications or services that are better adapted to changing technology or customer demands and that could render our products and services unmarketable or obsolete.

In addition, if the markets for computer-telephony applications, Internet Protocol network products, or related products fail to develop or continue to develop more slowly than we anticipate, or if we are unable for any reason to capitalize on any of these emerging market opportunities, our business, financial condition and operating results could be significantly harmed.

Our future success largely depends on increased commercial acceptance of our Inter-Tel 5000 Network Communications Solutions, Axxess® system, the Lake OfficeLink product (branded EncoreCX® in North America), speech recognition, Interactive Voice Response, presence management, collaboration, messaging products, Session Initiation Protocol (SIP) applications, and related computer-telephony products.

Over the past 18 to 24 months, we have introduced a number of new products and platforms, including: Unified Communicator® software, a web-based, speech-recognition, wireless PDA, and Wireless Application Protocol (WAP) software application for controlling and managing calls, contacts and presence status; Enterprise® Conferencing and Enterprise® Instant Messaging software, a SIP-based web and audio conferencing application; Inter-Tel Webconferencing and Inter-Tel Remote support (collaboration) solutions; Model 8500 series digital endpoints; Model 8600 series Multi-protocol SIP endpoints; Inter-Tel Application Platform, a highly flexible speech-recognition, text-to-speech and CTI application generation platform; enhanced convergence features on the Axxess system, including support of standard Session Initiation Protocol (SIP) endpoints and trunk gateways; and several other telephony-related products. In recent history, sales of our Axxess business communications systems and related software have comprised a substantial portion of our net sales. Our future success depends, in large part, upon increased commercial acceptance and adoption of the products or platforms identified above, as well as the Axxess system, the Inter-Tel 5000 Network Communications products, the Application Platform, the Unified Communicator and related computer-telephony products, the Linktivity collaboration technology, the Lake Communications converged systems and software, SIP standards-based applications and devices, new speech recognition and Interactive Voice Response products, and future upgrades and enhancements to these products and networking platforms. We cannot assure you that these products or platforms will achieve commercial acceptance in the future.

Our products are complex and may contain errors or defects that are detected only after their release, which may cause us to incur significant unexpected expenses and lost sales.

Our telecommunications products and software are highly complex. Although our new products and upgrades are examined and tested prior to release, they can only be fully tested when used by a large customer base. Consequently, our customers have in the past and may in the future discover program errors, or "bugs," or other defects after new products and upgrades have been released. Some of these bugs may result from defects contained in component parts or software from our suppliers or other third parties that are intended to be compatible with our products and over which we have little or no control. Although we have test procedures and quality control standards in place designed to minimize the number of errors and defects in our products, we cannot assure you that our new products and upgrades will be free of bugs when released. If we are unable to quickly or successfully correct bugs identified after release, we could experience the following, any of which would harm our business:

- costs associated with the remediation of any problems;
- costs associated with design modifications;
- loss of or delay in revenues;

- loss of customers;
- damage to our reputation;
- failure to achieve market acceptance or loss of market share;
- increased service and warranty costs;

- liabilities to our customers; and
- increased insurance costs.

The complexity of our products could cause delays in the development and release of new products and services. As a result, customer demand for our products could decline, which could harm our business.

Due to the complexity of our products and software, we have in the past experienced and expect in the future to experience delays in the development and release of new products or product enhancements. If we fail to introduce new software, products or services in a timely manner, or fail to release upgrades to our existing systems or products and software on a regular and timely basis, customer demand for our products and software could decline, which would harm our business.

Business acquisitions, new business ventures, dispositions or joint ventures entail numerous risks and may disrupt our business, dilute shareholder value and distract management attention.

As part of our business strategy, we consider acquisitions of, or significant investments in, businesses that offer products, services and technologies complementary to ours. Such acquisitions could materially adversely affect our operating results and/or the price of our common stock. Acquisitions also entail numerous risks, some of which we have experienced and may continue to experience, including:

- unanticipated costs and liabilities;
- difficulty of assimilating the operations, products and personnel of the acquired business;
- difficulties in managing the financial and strategic position of acquired or developed products, services and technologies;
- difficulties in maintaining customer relationships;
- difficulties in servicing and maintaining acquired products, in particular where a substantial portion of the target's sales were derived from our competitor's products and services;
- difficulty of assimilating the vendors and independent contractors of the acquired business;
- the diversion of management's attention from the core business;
- inability to maintain uniform standards, controls, policies and procedures; and
- impairment of relationships with acquired employees and customers occurring as a result of integration of the acquired business.

In particular, in prior years our operating results were materially adversely affected by several of the factors described above, including substantial operating losses and impairment charges resulting from Executone and Inter-Tel.NET. Refer to Note C to the Condensed Consolidated Financial Statements for additional information concerning our acquisitions.

We completed two acquisitions in 2002, one acquisition and one technology investment in 2003, five acquisitions and one technology investment in 2004, and one acquisition in 2005. The 2002 acquisitions included certain assets and liabilities of an operating company and the stock of a United Kingdom technology company. In 2003, we acquired selected assets and assumed certain liabilities of a former Inter-Tel dealer and we acquired the rights to certain developed technology. In 2004, we acquired certain assets and assumed certain liabilities of four former Inter-Tel dealers. In addition, we completed one technology related acquisition, coupled with a license of technology in 2004. In March of 2005, we acquired all of the outstanding stock of Lake and its several related entities in Ireland. These entities are similar in nature to our wholesale operations and also include significant technology-related assets. These acquisitions are subject to risks and uncertainties including, but not limited to, those indicated above.

Finally, to the extent that shares of our stock or the rights to purchase stock are issued in connection with any future acquisitions, dilution to our existing shareholders will result and our earnings per share may suffer. Any future acquisitions may not generate additional revenue or provide any benefit to our business, and we may not achieve a satisfactory return on our investment in any acquired businesses.

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We may not be able to adequately protect our proprietary technology and may be infringing upon third-party intellectual property rights.

Our success depends in part upon protecting our proprietary technology. As of March 31, 2005, we held twenty-seven (27) U.S. patents for telecommunication and messaging products, systems and processes and had applied to the U.S. Patent and Trademark Office for fifteen (15) additional patents. We also rely on copyright and trade secret law and contractual provisions to protect our intellectual property. Despite these precautions, third parties could copy or otherwise obtain and use our technology without authorization, or develop similar technology independently.

Any patent, trademark or copyright that we own or have applied to own is subject to being invalidated, circumvented or challenged by a third party. Effective protection of intellectual property rights may be unavailable or limited in foreign countries. The telecommunications and networking industries are heavily patented and we cannot assure that the protection of our proprietary rights will be adequate or that competitors will not independently develop similar technology, duplicate our services or design around any patents or other intellectual property rights we hold. Litigation may be necessary in the future to enforce our intellectual property rights, to protect our trade secrets, to determine the validity and scope of the proprietary rights of others, or to defend against claims of infringement or invalidity. Litigation could be costly, absorb significant management time and harm our business.

Many of our competitors have large patent portfolios and we are subject to or could become subject to third party claims that our current or future products or services infringe upon the rights of others. For example, we are subject to claims initiated by Avaya and Lucent, two of our primary competitors, alleging that certain of our key products infringe upon their intellectual property rights, including patents, trademarks, copyrights or other intellectual property rights. We have viewed presentations from Avaya alleging that our Axxess business communications system and associated applications utilize inventions covered by certain of their patents. We have also made claims against Avaya for infringement of our patents. We are continuing the process of investigating these matters. The ultimate outcomes by their nature are uncertain and we cannot assure you that these matters, individually or collectively, would not have a material adverse impact on our financial position and future results of operations.

When any such claims are asserted against us, among other means to resolve the dispute, we may seek to license the third party's intellectual property rights. Purchasing such licenses can be expensive, and we cannot assure you that a license will be available on prices or other terms acceptable to us, if at all. Alternatively, we could resort to litigation to challenge such a claim. Litigation could require us to expend significant sums of cash and divert our management's attention. In the event a court renders an enforceable decision with respect to our intellectual property, we may be required to pay significant damages, develop non-infringing technology or acquire licenses to the technology subject to the alleged infringement. Any of these actions or outcomes could harm our business. If we are unable or choose not to license technology, or decide not to challenge a third party's rights, we could encounter substantial and costly delays in product introductions. These delays could result from efforts to design around asserted third party rights or our discovery that the development, manufacture or sale of products requiring these licenses could be foreclosed.

We have many competitors and expect new competitors to enter our market, which could increase price competition and spending on research and development and which may impair our ability to compete successfully.

The markets for our products and services are extremely competitive and we expect competition to increase in the future. Our current and potential competitors in our primary business segments include:

- PABX, converged systems and IP-PBX providers, distributors, or resellers such as Alcatel, Altigen, Avaya, Cisco Systems, Comdial, 3Com, EADS Telecom, Iwatsu, Interactive Intelligence, Lucky Goldstar, Mitel, NEC, Nortel, Panasonic, Samsung, ShoreTel, Siemens, Toshiba, Vertical Networks/ArtiSoft and Vodavi;
- large data routing and convergence companies such as 3Com, Adtran and Cisco Systems;
- voice processing applications providers such as ADC, InterVoice-Brite, Active Voice (a subsidiary of NEC

America), Avaya, and Captaris (formerly AVT);

- web collaboration product and service providers, such as Centra, eDial (a division of Alcatel), IBM, Microsoft, Raindance Communications, and WebEx;
- long distance services providers such as AT&T, MCI, Qwest and Sprint;

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- large computer and software corporations such as IBM, HP, Intel and Microsoft;
- regional Bell operating companies, or RBOCs, competitive local exchange companies (CLECs); cable television companies, IP Centrex service providers, and satellite and other wireless and wireline broadband service providers offering IP centrex services such as AT&T, Covad, Level-3, Qwest, SBC, and Time-Warner Telecom; and
- independent leasing companies that provide telecom equipment financing.

These and other companies may form strategic relationships with each other to compete with us. These relationships may take the form of strategic investments, joint-marketing agreements, licenses or other contractual arrangements. Strategic relationships and business combinations could increase our competitors' ability to address customer needs with their product and service offerings.

Many of our competitors and potential competitors have substantially greater financial, customer support, technical and marketing resources, larger customer bases, longer operating histories, greater name recognition and more established relationships in the industry than we do. We cannot be sure that we will have the resources or expertise to compete successfully. Compared to us, our competitors may be able to:

- develop and expand their product and service offerings more quickly;
- offer greater price discounts or make substantial product promotions;
- adapt to new or emerging technologies and changing customer needs faster;
- take advantage of acquisitions and other opportunities more readily;
- negotiate more favorable licensing agreements with vendors;
- devote greater resources to the marketing and sale of their products; and
- address customers' service-related issues more adequately.

Some of our competitors may also be able to provide customers with additional benefits at lower overall costs or to reduce their gross margins aggressively in an effort to increase market share. We cannot be sure we will be able to match cost reductions by our competitors. In recent periods, due to competitive pressures, we have discounted pricing on our telephone systems and offered promotions. In addition, we believe there is likely to be further consolidation in our markets, which could lead to having even larger and more formidable competition and other forms of competition that could cause our business to suffer.

Our reliance on a limited number of suppliers for key components and our dependence on contract manufacturers could impair our ability to manufacture and deliver our products and services in a timely and cost-effective manner.

We currently obtain certain key components for our digital communication platforms, including certain microprocessors, integrated circuits, power supplies, voice processing interface cards and IP telephony cards, from a limited number of suppliers and manufacturers. Our reliance on these limited suppliers and contract manufacturers involves risks and uncertainties, including the possibility of a shortage or delivery delay for some key components. We currently manufacture our products, including products manufactured for Lake, through third-party subcontractors located in the United States, Mexico, the People's Republic of China and the United Kingdom. Foreign manufacturing facilities are subject to changes in governmental policies, imposition of tariffs and import restrictions and other factors beyond our control. We have experienced occasional delays in the supply of components and finished goods that have harmed our business. If inventory levels are not adequately maintained and managed we are at risk of not having the appropriate inventory quantities on hand to meet sales demand. We may experience similar delays in the future.

Our reliance on third party manufacturers and OEM partners involves a number of additional risks, including reduced control over delivery schedules, quality assurance and costs. Our business may be harmed by any delay in delivery or any shortage of supply of components or finished goods from a supplier caused by any number of factors, including but not limited to the acquisition of the vendor by another company (which has recently occurred with one of our primary suppliers). Our business may also be harmed if we are unable to develop alternative or additional supply sources as necessary. To date, we have been able to obtain supplies of components and products in a timely manner even though we do not have long-term supply contracts with any of our contract manufacturers. However, we cannot assure you we will be able to continue to obtain components or finished goods in sufficient quantities or quality or on favorable pricing or delivery terms in the future.

We derive a substantial portion of our net sales from our dealer network and if these dealers do not effectively promote and sell our products, our business and operating results could be harmed.

We derive a substantial portion of our net sales through our network of independent dealers. We face intense competition from other telephone, voice processing, and voice and data router system manufacturers for these dealers' business, as most of our dealers carry other products that compete with our products. Our dealers may choose to promote the products of our competitors to our detriment. We have developed programs and expended capital as incentives to our dealers to promote our products, and we cannot assure you that these techniques will continue to be successful. The loss of any significant dealer or group of dealers, or any event or condition harming our dealer network, could harm our business, financial condition and operating results.

We have been the subject of government investigations, which have resulted in convictions and civil penalties and may cause further competitive and financial harm to our business.

On January 5, 2005, the Company received court approval of a civil settlement agreement (the "Civil Settlement") and a criminal plea agreement (the "Plea Agreement") with the United States of America, each dated as of December 8, 2004 and disclosed on that same date. The court approval of the Civil Settlement and Plea Agreement resolves the investigation of the Department of Justice into the participation of Inter-Tel Technologies, Inc., the Company's wholly-owned subsidiary ("Technologies") in a federally administered "E-Rate program" to connect schools and libraries to the Internet. In connection with the Civil Settlement, Technologies agreed to pay a penalty of $6,740,450 and forego the collection of certain accounts receivable of $259,540 related to Technologies' participation in the E-Rate program. In connection with the Plea Agreement, Technologies entered guilty pleas to charges of mail fraud and an antitrust violation. Under the Plea Agreement, Technologies agreed to pay a fine of $1,721,000 and observe a three-year probationary period, which will, among other things, require Technologies to implement a comprehensive corporate compliance program. The penalties and fines described above were paid during the first quarter of 2005.

In addition, on January 21, 2005, Inter-Tel Technologies received notification from the Federal Communications Commission that Technologies was temporarily suspended from participation in the E-Rate program pending a proposed debarment. Technologies has contested the scope and length of the proposed debarment from the E-Rate program, but there can be no assurance that Technologies will be successful in this regard. Revenues in 2004 relating to Technologies' participation in the E-Rate program were not significant.

The existence and disclosure of the Civil Settlement, Plea Agreement and FCC Notice may have already caused competitive harm to Inter-Tel, and these matters may further harm Inter-Tel's business.

Inter-Tel is also subject to litigation in the ordinary course of business. We cannot assure you that any adverse outcome in connection with such litigation would not impair our business or financial condition.

Managing our international sales efforts may expose us to additional business risks, which may result in reduced sales or profitability in our international markets.

We are currently expending resources to maintain and expand our international dealer network in the countries in which we already have a presence and in new countries and regions. International sales are subject to a number of risks, including changes in foreign government regulations and telecommunication standards, export license requirements, tariffs and taxes, other trade barriers, difficulties in protecting our intellectual property, fluctuations in currency exchange rates, difficulty in collecting receivables, difficulty in staffing and managing foreign operations, and political and economic instability. In particular, the terrorist acts of September 11, 2001, continued hostilities in Iraq and turmoil in the Middle East and North Korea have created an uncertain international economic environment and we cannot predict the impact of these acts, any future terrorist acts or any related military action on our efforts to expand our international sales. Fluctuations in currency exchange rates could cause our products to become relatively more expensive to customers in a particular country, leading to a reduction in sales or profitability in that country. In addition,

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the costs associated with developing international sales or an international dealer network may not be offset by increased sales in the short term, or at all. Any of these risks could cause our products to become relatively more expensive to customers in a particular country, leading to reduced sales or profitability in that country.

During the past year, Inter-Tel has been in the process of establishing a new dealer relationship in South Africa and launched that relationship in 2005. It is possible that this business many not materialize as soon as expected and may require additional support expenses to reach the expected revenue levels.

In December 2004, we wrote off our Japan operations. As a result, Inter-Tel assigned selected assets and the customer base of the Inter-Tel Japan direct sales office to a new dealer in Japan that will sell and support Inter-Tel products to our Japan customers. We may continue to incur expenses related to the winding down of our direct presence over the next few quarters.

The Lake acquisition closed in March 2005. Among other acquisition-related risks, we face risks of deterioration of international sales during the integration process, loss of key customers or that projected growth could be delayed or may not materialize at all.

If we lose key personnel or are unable to hire additional qualified personnel as necessary, we may not be able to achieve our objectives.

We depend on the continued service of, and our ability to attract and retain, qualified technical, marketing, sales and managerial personnel, many of whom would be difficult to replace. Competition for qualified personnel is intense, and we have historically had difficulty in hiring employees in the timeframe we desire, particularly skilled engineers or sales personnel. The loss of any of our key personnel or our failure to effectively recruit additional key personnel could make it difficult for us to manage our business, complete timely product introductions or meet other critical business objectives. Moreover, our operating results could be impaired if we lose a substantial number of key employees from recent acquisitions, including personnel from acquisitions identified in Note B to the Consolidated Financial Statements. We cannot assure you we will be able to continue to attract and retain the qualified personnel necessary for the development of our business.

Our IP network products may be vulnerable to viruses, other system failure risks and security concerns, which may result in lost customers or slow commercial acceptance of our IP network products.

Inter-Tel's IP telephony and network products may be vulnerable to computer viruses or similar disruptive problems. Computer viruses or problems caused by third parties could lead to interruptions, delays or cessation of service that could harm our operations and revenues. In addition, we may lose customers if inappropriate use of the Internet or other IP networks by third parties jeopardizes the security of confidential information, such as credit card or bank account information or the content of conversations over the IP network. In addition, user concerns about privacy and security may cause IP networks in general to grow more slowly, and impair market acceptance of our IP network products in particular, until more comprehensive security technologies are developed and deployed industry-wide.

We may be unable to achieve or manage our growth effectively, which may harm our business.

The ability to operate our business in an evolving market requires an effective planning and management process. Our efforts to achieve growth in our business have placed, and are expected to continue to place, a significant strain on our personnel, management systems, infrastructure and other resources. In addition, our ability to manage any potential future growth effectively will require us to successfully attract, train, motivate and manage new employees, to integrate new employees into our overall operations and to continue to improve our operational, financial and management controls and procedures. Furthermore, we expect we will be required to manage an increasing number of relationships with suppliers, manufacturers, customers and other third parties. If we are unable to implement adequate controls or integrate new employees into our business in an efficient and timely manner, our operations could be adversely affected and our growth could be impaired.

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The introduction of new products and services has lengthened our sales cycles, which may result in significant sales and marketing expenses.

In the past few years, we introduced IP telephony enhancements to the Axxess® system as well as presence management and collaboration applications, which are typically sold to larger customers at a higher average selling price and often represent a significant expenditure in communications infrastructure by the prospective enterprise customer. Accordingly, the purchase of our products typically involves numerous internal approvals relating to the evaluation, testing, implementation and acceptance of new technologies. This evaluation process frequently results in a lengthy sales process, which can range from a few months to more than 12 months, thereby subjecting our sales cycle to a number of significant uncertainties concerning budgetary constraints and internal acceptance reviews. The length of our sales cycle also may vary substantially from customer to customer and along product lines. While our customers are evaluating our products before placing an order with us, we may incur substantial sales and marketing expenses and expend significant management effort. In addition, installation of multiple systems for large, multi-site customers may occur over an extended period of time, and depending on the contract terms with these customers, revenues may be recognized over more than one quarter, as systems are completed in separate phases and accepted by the customers. Consequently, if sales forecasted from a specific customer for a particular quarter are not realized in that quarter, our operating results could be materially adversely affected.

We rely heavily upon third-party packaged software systems to manage and run our business processes and to produce our financial statements. From time to time we upgrade these systems to ensure continuation of support and to expand the functionality of the systems to meet our business needs. The risks associated with the upgrade process include disruption of our business processes, which could harm our business.

We currently run third-party applications for data processing in our distribution center operations, shipping, materials movement, customer service, invoicing, financial record keeping and reporting, and for other operations and administrative functions. The nature of the software industry is to upgrade software systems to make architectural changes, increase functionality, improve controls and address software bugs. Over time, older versions of the software become less supported or unsupported by our vendors for financial and other reasons and eventually become obsolete. Oracle, the primary supplier of our third-party applications, provides notice of the dates that Oracle will de-support the software and companies are expected to either make plans to upgrade to newer versions or operate without Oracle support. While Oracle and other third-party vendors may provide advanced notice of product upgrade schedules and take other steps to make the upgrade process as straightforward as possible, we are subject to risks associated with the process, and in some cases we may choose to continue to utilize and maintain the unsupported third-party software using our own information systems personnel. Our software systems could become unstable following an upgrade process and impact our ability to process data properly in these systems, including timely and accurate shipment of products, invoicing our customers properly and the production of accurate and timely financial statements. There are risks associated with failing to apply necessary security upgrades intended to resolve vulnerabilities. While we strive to take necessary precautions and properly test security-related upgrades before applying these upgrades, we must weigh the risks of not applying the upgrade against the risks of vulnerabilities being exploited for malicious purposes by an outside entity. Should a security vulnerability be exploited, our systems could become unstable and/or data could be compromised, thereby adversely affecting our business. We expect to affect software upgrades in the future and cannot assure you these software upgrades or enhancements will operate as intended or be free from bugs or that we will be able to operate effectively using unsupported third-party software using our existing personnel and resources. If we are unable to successfully integrate new software into our information systems, our operations, customer service and financial reporting could be adversely affected and could harm our business.

Our stock price has been and may continue to be volatile, impairing your ability to sell your shares at or above purchase price.

The market price for our common stock has been highly volatile. The volatility of our stock could be subject to continued wide fluctuations in response to many risk factors listed in this section, and others beyond our control, including:

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- announcements of developments relating to our business;
- fluctuations in our operating results;
- the impact of our dividend announcements, repurchase program or sales of stock by officers and directors;
- shortfalls in revenue or earnings relative to securities analysts' expectations;
- announcements of technological innovations or new products or enhancements by us or our competitors, including product delays;
- announcements of acquisitions or planned acquisitions of other companies or businesses;
- investors' reactions to acquisition announcements or any forecasts of our future results;
- general economic conditions in the telecommunications industry;
- the market for Internet-related voice and data products and services;
- changes in the national or worldwide economy;
- changes in legislation or regulation affecting the telecommunications industry;
- developments relating to our intellectual property rights and the intellectual property rights of third parties;
- litigation or governmental investigations of our business practices;
- the impact of the E-Rate settlement and possible FCC debarment, which could affect both our government business and our commercial business.
- changes in our relationships with our customers and suppliers, including shipping and manufacturing problems associated with subcontracted vendors;
- national and regional weather patterns; and
- threats of or outbreaks of war, hostilities, terrorist acts or other civil disturbances;

In addition, stock prices of technology companies in general, and for voice and data communications companies in particular, have experienced extreme price fluctuations in recent years which have often been unrelated to the operating performance of affected companies. We cannot assure you the market price of our common stock will not experience significant fluctuations in the future, including fluctuations unrelated to our performance.

Our Chairman of the Board of Directors, CEO and President controls 19.4% of our Common Stock and is able to significantly influence matters requiring shareholder approval.

As of March 31, 2005, Steven G. Mihaylo, Inter-Tel's Chairman of the Board of Directors, Chief Executive Officer and President, beneficially owned approximately 19.4% of the existing outstanding shares of the common stock of Inter-Tel. As a result, he has the ability to exercise significant influence over all matters requiring shareholder approval. In addition, the concentration of ownership could have the effect of delaying or preventing a change in control of Inter-Tel.

Changes in stock option accounting rules may adversely impact our reported operating results prepared in accordance with generally accepted accounting principles, our stock price and our competitiveness in the employee marketplace.

Technology companies like ours have a history of using broad based employee stock option programs to hire, provide incentives for and retain our workforce in a competitive marketplace. Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" ("SFAS 123") allowed companies the choice of either using a fair value method of accounting for options, which would result in expense recognition for all options granted, or using an intrinsic value method, as prescribed by Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" (APB 25), with a pro forma disclosure of the impact on net income (loss) of using the fair value option expense recognition method. We have elected to apply APB 25 and accordingly we generally do not recognize any expense with respect to employee stock options as long as such options are granted at exercise prices equal to the fair value of our Common Stock on the date of grant.

In December 2004, the FASB issued Statement No. 123 (revised 2004), Share-Based Payment ("SFAS 123R"), which replaces SFAS No. 123, Accounting for Stock-Based Compensation, (SFAS 123) and supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees. SFAS 123R requires all share-based payments to employees, including grants of employee stock options and employee stock purchase plan shares, to be recognized in the financial statements based on their fair values beginning with

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the Company's fiscal year beginning January 1, 2006. The pro forma disclosures previously permitted under SFAS 123 no longer will be an alternative to financial statement recognition.

Under SFAS 123R, we must determine the appropriate fair value model to be used for valuing share-based payments, the amortization method for compensation cost and the transition method to be used at date of adoption. The transition methods include prospective and retroactive adoption options. Under the retroactive option, prior periods may be restated either as of the beginning of the year of adoption or for all periods presented. The prospective method requires that compensation expense be recorded for all unvested stock options and restricted stock at the beginning of the first quarter of adoption of SFAS 123R, while the retroactive methods would record compensation expense for all unvested stock options and restricted stock beginning with the first period restated. We are evaluating the requirements of SFAS 123R and expect that the adoption of SFAS 123R will have a material impact on our consolidated results of operations and earnings per share.

We have not yet determined the method of adoption or the effect of adopting SFAS 123R, and we have not determined whether the adoption will result in amounts that are similar to the current pro forma disclosures under SFAS 123. In addition, this new statement could impact our ability to utilize broad-based employee stock plans to reward employees and could result in a competitive disadvantage to us in the employee marketplace.

Risks Related to Our Industry

Reductions in spending on enterprise communications equipment may materially and adversely affect our business.

The overall economic slowdown of the last several years has had and may continue to have a harmful effect on the market for enterprise communications equipment. Our customers have reduced significantly their capital spending on communications equipment in an effort to reduce their own costs and bolster their revenues. The market for enterprise communications equipment may only grow at a modest rate or possibly not grow at all, and our financial performance has been and may continue to be materially and adversely affected by the reductions in spending on enterprise communications equipment.

The emerging market for IP network telephony is subject to market risks and uncertainties that could cause significant delays and expenses.

The market for IP network voice communications products has begun to develop only recently, is evolving rapidly and is characterized by an increasing number of market entrants who have introduced or developed products and services for Internet or other IP network voice communications. As is typical of a new and rapidly evolving industry, the demand for and market acceptance of, recently introduced IP network products and services are highly uncertain. We cannot assure you that IP voice networks will become widespread. Even if IP voice networks become more widespread in the future, we cannot assure that our products, including the IP telephony features of the *Axxess* systems and Inter-Tel 5000 Network Communication Solutions, our IP endpoints and IP applications will successfully compete against other market players and attain broad market acceptance.

Moreover, the adoption of IP voice networks and importance of development of products using industry standards such as MGCP and SIP, generally require the acceptance of a new way of exchanging information. In particular, enterprises that have already invested substantial resources in other means of communicating information may be reluctant or slow to adopt a new approach to communications. If the market for IP network voice communications fails to develop or develops more slowly than we anticipate, our IP network telephony products could fail to achieve market acceptance, which in turn could significantly harm our business, financial condition and operating results. This growth may be inhibited by a number of factors, such as quality of infrastructure; security concerns; equipment, software or other technology failures; regulatory encroachments; inconsistent quality of service; poor voice quality over IP networks as compared to circuit-switched networks; and lack of availability of cost-effective, high-speed network capacity. Moreover, as IP-based data communications and telephony usage grow, the infrastructure used to support these IP networks, whether public or private, may not be able to support the demands placed on them and their performance or reliability may decline. The technology that allows voice and facsimile

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communications over the Internet and other data networks, and the delivery of other value-added services, is still in the early stages of development.

Government regulation of third party long distance and network service entities on which we rely may harm our business.

Our supply of telecommunications services and information depends on several long distance carriers, RBOCs, local exchange carriers, or LECs, and competitive local exchange carriers, or CLECs. We rely on these carriers to provide local and long distance services, including voice and data circuits, to our customers and to provide us with billing information. Long distance services are subject to extensive and uncertain governmental regulation on both the federal and state level. We cannot assure you that the increase in regulations will not harm our business. Our current contracts for the resale of services through long distance carriers include multi-year periods during which we have minimum use requirements and/or costs. The market for long distance services is experiencing, and is expected to continue to experience significant price competition, and this may cause a decrease in end-user rates. We cannot assure you that we will meet minimum use commitments, that we will be able to negotiate lower rates with carriers if end-user rates decrease or that we will be able to extend our contracts with carriers at favorable prices. If we are unable to secure reliable Network Services from certain long distance carriers, RBOCs, LECs and CLECs, or if these entities are unwilling or unable to provide telecommunications services and billing information to us on favorable terms, our ability to expand our own Network Services will be harmed. Carriers that provide telecommunications services to us may also experience financial difficulties, up to and including bankruptcies, which could harm our ability to offer telecommunications services.

Consolidation within the telecommunications industry could increase competition and adversely affect our business.

There has been a trend in the telecommunications industry toward consolidation and we expect this trend to continue as the industry evolves. As a result of this consolidation trend, new stronger companies may emerge that have improved financial resources, enhanced research and development capabilities and a larger and more diverse customer base. The changes within the telecommunications industry may adversely affect our business, operating results and financial condition.

Terrorist activities and resulting military and other actions could harm our business.

Terrorist attacks in New York and Washington, D.C. in September of 2001 disrupted commerce throughout the world. The continued threat of terrorism, the conflict in Iraq and the potential for additional military action and heightened security measures in response to these threats may continue to cause significant disruption to commerce throughout the world. To the extent that disruptions result in a general decrease in corporate spending on information technology or advertising, our business and results of operations could be harmed. We are unable to predict whether the conflict in Iraq and its aftermath, the threat of terrorism or the responses thereto will result in any long-term commercial disruptions or if such activities or responses will have a long-term adverse effect on our business, results of operations or financial condition. Additionally, if any future terrorist attacks were to affect the operation of the Internet or key data centers, our business could be harmed. These and other developments arising out of the potential attacks may make the occurrence of one or more of the factors discussed herein more likely to occur.

We Are Exposed To Increased Costs And Risks Associated With Compliance With Changing Laws, Regulations And Standards In General, and Specifically With Increased And New Regulation Of Corporate Governance And Disclosure Standards.

We are spending an increased amount of management time and external resources to comply with existing and changing laws, regulations and standards in general, and specifically relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, new SEC regulations, PCAOB and Nasdaq Stock Market rules, as well as commercial dealings with other government entities. In particular, Section 404 of the Sarbanes-Oxley Act of 2002 requires management's annual review and

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evaluation of our internal control systems, and attestations of the effectiveness of these systems by our management and by our independent auditors. We have completed our documentation and testing of our internal control systems and procedures for 2004. This process required us to hire additional personnel and use outside advisory services and resulted in additional accounting and legal expenses. The results of the documentation and testing for 2004 indicate that we currently have adequate internal controls over financial reporting; however, if in the future our chief executive officer, chief financial officer or independent auditors determine that our controls over financial reporting are not effective as defined under Section 404, investor perceptions of Inter-Tel may be adversely affected and could cause a decline in the market price or our stock. Failure to comply with other existing and changing laws, regulations and standards could also adversely affect the Company.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The following discussion about our market risk disclosures involves forward-looking statements. Actual results could differ materially from those projected in the forward-looking statements. We are exposed to market risk related to changes in interest rates and foreign currency exchange rates. We do not use derivative financial instruments.

INVESTMENT PORTFOLIO. We do not use derivative financial instruments in our non-trading investment portfolio. Inter-Tel maintains a portfolio of highly liquid cash equivalents typically maturing in three months or less as of the date of purchase. Inter-Tel places its investments in instruments that meet high credit quality standards, as specified in our investment policy guidelines.

The Company also maintains short-term and long-term investments. Those investments that are classified as available for sale have been recorded at fair value, which approximates cost. Those investments that are classified as held-to-maturity have been recorded at cost and amortized to face value. Short-term investments include certificates of deposit, auction rate certificates, auction rate preferred securities, municipal preferred securities, federal agency issues and mutual funds. The auction rate securities are adjustable-rate securities with dividend rates that are reset periodically by bidders through periodic "Dutch auctions" generally conducted every 7 to 49 days by a trust company or broker/dealer on behalf of the issuer. The Company believes these securities are highly liquid investments through the related auctions; however, the collateralizing securities have stated terms of up to thirty-four (34) years. The long-term investments consist of federal agency issues. Both the short-term and long-term instruments are rated A or higher by Standard & Poor's Ratings Group, or equivalent. The Company's investments are intended to establish a high-quality portfolio that preserves principal, meets liquidity needs, avoids inappropriate concentrations and delivers an appropriate yield in relationship to the Company's investment guidelines and market conditions. Given the short-term nature of the majority of these investments, and that we have no borrowings outstanding, we are not subject to significant interest rate risk.

LEASE PORTFOLIO. We offer to our customers lease financing and other services, including our Total Solutions program, through our Inter-Tel Leasing subsidiary. We fund these programs in part through the sale to financial institutions of rental payment streams under the leases. Upon the sale of the rental payment streams, we continue to service the leases and maintain limited recourse on the leases. We maintain reserves for loan losses on all leases based on historical loss experience, past due accounts and specific account analysis. Although to date we have been able to resell the rental streams from leases under our lease programs profitably and on a substantially current basis, the timing and profitability of lease resales could impact our business and operating results, particularly in an environment of fluctuating interest rates and economic uncertainty. If we were required to repurchase rental streams and realize losses thereon in amounts exceeding our reserves, our operating results could be materially adversely affected. See "Liquidity and Capital Resources" and "Critical Accounting Policies and Estimates" in Management's Discussion and Analysis for more information regarding our lease portfolio and financing.

IMPACT OF FOREIGN CURRENCY RATE CHANGES. We invoice the customers of our international subsidiaries primarily in the local currencies of our subsidiaries for product and service revenues. Inter-Tel is exposed to foreign exchange rate fluctuations as the financial results of foreign subsidiaries are translated into U.S. dollars in consolidation. The impact of foreign currency rate changes have historically been insignificant.

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ITEM 4. CONTROLS AND PROCEDURES

Evaluation of disclosure controls and procedures. Except as discussed in the following paragraph, our management evaluated, with the participation of our Chief Executive Officer and our Chief Financial Officer, the design and operation of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the "Exchange Act") as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on this evaluation, our management, including our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures are designed, and are effective to give reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and to ensure that information required to be disclosed in the reports filed or submitted under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, in a manner that allows timely decisions regarding required disclosure.

On February 28, 2005, the Company completed the acquisition of Lake. The recorded cost of the acquisition including capitalized transaction costs was $28.7 million. Net revenues from the Lake subsidiary included in the consolidated net income for the quarter were $2.6 million. See Note C to the Condensed Consolidated Financial Statements for further discussion of this acquisition. We have not completed our evaluation of the design and operation of the disclosure controls and procedures for this consolidated subsidiary as of March 31, 2005. We expect to complete such evaluation prior to the end of 2005.

Changes in internal controls over financial reporting. There were no changes in our internal controls over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal controls over financial reporting.

INTER-TEL, INCORPORATED AND SUBSIDIARIES

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are involved from time to time in litigation incidental to our business. We believe that the outcome of current litigation will not have a material adverse effect upon our business, financial condition or results of operations and will not disrupt our normal operations.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

Board Authorization to Repurchase up to $75 Million of Inter-Tel Stock. On February 15, 2005, Inter-Tel announced that its Board of Directors approved a stock repurchase program, with no stated expiration date, in which Inter-Tel may purchase up to $75 million of its Common Stock in the open market from time to time, depending upon general market conditions, the Company's share price, the level of employee stock option exercises, the level of employee stock purchase plan purchases, the availability of funds and other factors. While the Company has made and intends to continue to make repurchases in subsequent periods, no Common Stock was repurchased pursuant to the Plan during the Company's first fiscal quarter of 2005.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES — Not Applicable

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS—Not Applicable

ITEM 5. OTHER INFORMATION — Not Applicable

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ITEM 6. EXHIBITS:

Exhibit 10:	Share Purchase Agreement, signed February 28, 2005
Exhibit 31.1:	Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibit 31.2:	Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibit 32.1:	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
Exhibit 32.2:	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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.

INTER-TEL, INCORPORATED

May 10, 2005

/s/ Steven G. Mihaylo
Steven G. Mihaylo
Chairman of the Board, Chief Executive
Officer and President

May 10, 2005

/s/ Kurt R. Kneip
Kurt R. Kneip
Senior Vice President and
Chief Financial Officer

E - Arizona Projections

A. Projected total intrastate revenue for the first 12 months of service: $1,000

B. Projected value of total intrastate operating expenses for the first 12 months of service: $800.00

C. Projected net book value of all Arizona jurisdictional assets to be used to provide telecommunications services to Arizona customers for the first 12 months of service: $100.00

D. Current net book value: $0.00