ALASKA COMMUNICATIONS SYSTEMS GROUP INC
Form 10-K
March 09, 2009

Table of Contents

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

(Mark One)

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

For the fiscal year ended December 31, 2008

OR

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

For the transition period from to

Commission file number 000-28167

Alaska Communications Systems Group, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**52-2126573**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

600 Telephone Avenue Anchorage, Alaska	**99503-6091**
(Address of principal executive offices)	(Zip Code)

(907) 297-3000

(Registrant s telephone number, including area code)

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

Title of each class	**Name of each exchange on which registered**
Common Stock, Par Value $.01 per Share	The NASDAQ Stock Market LLC

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

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

Yes o No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes o No þ

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes þ No o

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

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

Large accelerated filer o	Accelerated filer þ	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).
Yes o No þ

The aggregate market value of the shares of all classes of voting stock of the registrant held by non-affiliates of the registrant on June 30, 2008 was approximately $516 million computed upon the basis of the closing sales price of the Common Stock on that date. For purposes of this computation, shares held by directors (and shares held by any entities in which they serve as officers) and officers of the registrant have been excluded. Such exclusion is not intended; nor shall it be deemed, to be an admission that such persons are affiliates of the registrant.

As of February 20, 2009 there were outstanding 43,726,399 shares of Common Stock, $.01 par value, of the registrant.

Documents Incorporated by Reference

Portions of Registrant s definitive proxy statement for its annual stockholders meeting to be held on June 12, 2009 are incorporated by reference in Part III of this Form 10-K

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
ANNUAL REPORT ON FORM 10-K
FOR THE YEAR ENDED DECEMBER 31, 2008

		Page
PART I		
Item 1.	Business	3
Item 1A.	Risk Factors	16
Item 1B.	Unresolved Staff Comments	23
Item 2.	Properties	24
Item 3.	Legal Proceedings	24
Item 4.	Submission of Matters to a Vote of Security Holders	24
PART II		
Item 5.	Market for Registrant s Common Equity and Related Stockholder Matters	24
Item 6.	Selected Financial Data	26
Item 7.	Management s Discussion and Analysis of Financial Condition and Results of Operations	26
Item 7A.	Quantitative and Qualitative Disclosures About Market Risk	41
Item 8.	Financial Statements and Supplementary Data	43
Item 9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	43
Item 9A.	Controls and Procedures	43
Item 9B.	Other Information	43
PART III		
Item 10.	Directors and Executive Officers of the Registrant	44
Item 11.	Executive Compensation Summary Compensation Table	44
Item 12.	Security Ownership of Certain Beneficial Owners and Management and related Stockholder Matters	44
Item 13.	Certain Relationships and Related Transactions	45
Item 14.	Principal Accounting Fees and Services	45
PART IV		
Item 15.	Exhibits and Financial Statement Schedules	46
SIGNATURES		49
Index to Consolidated Financial Statements		F-1

EX-21.1
EX-23.1
EX-31.1
EX-31.2
EX-32.1

EX-32.2

2

Table of Contents

PART I

Item 1. Business

Forward Looking Statements and Analysts Reports

This Form 10-K and future filings by Alaska Communications Systems Group, Inc. and its consolidated subsidiaries (we , our , us , the Company and ACS Group) on Forms 10-K, 10-Q and 8-K and the documents incorporated therein by reference include 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. We intend such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements in these provisions. All statements other than statements of historical fact are forward-looking statements for purposes of federal and state securities laws, including statements about anticipated future operating and financial performance, financial position and liquidity, growth opportunities and growth rates, pricing plans, acquisition and divestiture opportunities, business prospects, strategic alternatives, business strategies, regulatory and competitive outlook, investment and expenditure plans, financing needs and availability and other similar forecasts and statements of expectation and statements of assumptions underlying any of the foregoing. Words such as aims , anticipates , believes , could , estimates , expects , hopes , intends , may , plans , projects , seeks , should and variations of the expressions are intended to identify these forward-looking statements. These forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from our historical experience and our present expectations or projections. Forward-looking statements by us are based on estimates, projections, beliefs and assumptions of management and are not guarantees of future performance. Such forward-looking statements may be contained in this Form 10-K under Item 1A Risk Factors and Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations and elsewhere. Actual future performance, outcomes and results may differ materially from those expressed in forward-looking statements made by us as a result of a number of important factors. Examples of these factors include (without limitation):

- our strongly competitive environment, which comprises national and local wireless and wireline facilities-based competitors;

- our ability to complete, manage, integrate, market, maintain and attract sufficient customers to our Northstar and Alaska-Oregon Network (AKORN) long-haul fiber facilities and our ability to develop attractive integrated products and services making use of the facility;

- the continued availability of financing in the amounts, at the terms, and subject to the conditions necessary, to support our future business;

- our ability to generate sufficient earnings and cash flows to continue to make dividend payments to our stockholders;

- rapid technological developments and changes in the telecommunications industries;

- changes in revenue resulting from regulatory actions affecting inter-carrier compensation;

- regulatory limitations on our ability to change our pricing for communications services;

- possible widespread or lengthy failures of our system or network cables, particularly our non-redundant systems, including our primary fiber-link connecting Alaska and the lower 48 states, which would cause significant delays or interruptions of service and/or loss of customers;

- other unanticipated damage to one or more of our high capacity cables resulting from construction or digging mishaps, fishing boats or natural disasters;

- changes in revenue from Universal Service Funds (USFs);
- the possible unavailability, beginning during the fiscal year 2009, of Statement of Financial Accounting Standard (SFAS) No. 71, Accounting for the Effects of Certain Types of Regulation, to our wireline subsidiaries or other changes in accounting policies or practices adopted voluntarily or as required by accounting principles generally accepted in the United States;
- changes in the demand for our products and services;
- changes in general industry and market conditions and growth rates;
- changes in interest rates or other general national, regional or local economic conditions;
- governmental and public policy changes;
- the success of any future acquisitions; and
- the matters described under Item 1A Risk Factors .

In light of these risks, uncertainties and assumptions, you should not place undue reliance on any forward-looking statements. Additional risks that we may currently deem immaterial or that are not currently known to us could also cause the forward-looking events discussed in this Form 10-K not to occur as described. Except as otherwise required by applicable

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securities laws, we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events, changed circumstances or any other reason after the date of this Form 10-K.

Investors should also be aware that while we do, at various times, communicate with securities analysts, it is against our policy to disclose to them any material non-public information or other confidential information. Accordingly, investors should not assume that we agree with any statement or report issued by an analyst irrespective of the content of the statement or report. To the extent that reports issued by securities analysts contain any projections, forecasts or opinions, such reports are not our responsibility.

Unless the context indicates otherwise, all references in this Form 10-K to we , our , ours , us , the company , ACS refer to Alaska Communications Systems Group, Inc. and its consolidated subsidiaries.

About ACS

We believe we provide Alaska s leading integrated communications services. We provide both wireline and wireless communications services throughout Alaska and we connect our networks to the lower 48 states via high-speed fiber optic cables. Our wireline business comprises one of the most expansive networks in Alaska. Our wireless business includes the largest third generation (3G) wireless network operating in Alaska today. Both segments rely on our highly skilled workforce of approximately 1,000 employees.

ACS was incorporated in 1998 under the laws of the State of Delaware. We began doing business as ACS in May 1999 following our acquisition of the Anchorage Telephone Utility and CenturyTel s Alaska assets.

Our principal executive offices are located at 600 Telephone Avenue, Anchorage, Alaska 99503. Our telephone number is (907) 297-3000.

Business Segments

We have two reportable business segments, wireline and wireless, which conduct the following principal activities:

Wireline: We provide communications services including voice, data, broadband, multi-protocol label switching (MPLS) services, network access, long distance and other services to consumers, carriers, businesses and government customers throughout Alaska and to and from Alaska.

Wireless: We provide wireless voice and data service and products and other value-added services and equipment sales across Alaska.

For a detailed review of our financial performance and results of operations by business segment, see Part II Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations and Note 17 Business Segments of our Consolidated Financial Statements , each of which are incorporated herein by reference.

Wireline

We provide voice, data, broadband, network access, long distance, and other advanced IP network services to consumers, carriers, businesses and government customers throughout Alaska and to and from Alaska. We provide telephone and high-speed Internet services to consumers in our wireline footprint. Our high-speed data network relies on advanced packet-based MPLS technology. Our MPLS network provides the framework for our Metro Ethernet service, which we market to medium and large businesses and government customers. Metro Ethernet offers our customers scalable, high-speed data and customized information technology products and services, as well as Internet connectivity.

Interstate and Enterprise Products and Services

During 2008, we acquired Crest Communications Corporation (Crest), and its extensive high-speed fiber optic cable system, which includes, Northstar, an undersea fiber system of approximately 1,900 miles with cable landing facilities in Whittier, Juneau, and Valdez, Alaska, and Nedonna Beach, Oregon. Crest s system also includes terrestrial transport components linking Nedonna Beach, Oregon to the Network Operations Control Center (NOCC) in Hillsboro, Oregon and collocation facilities in Portland, Oregon and Seattle, Washington.

We also have nearly completed construction of AKORN, a new state-of-the-art undersea fiber optic cable also connecting Alaska with the lower 48 states along a diverse path. We expect to commercially deploy AKORN in 2009.

Lastly, we deployed redundant NOCCs in Alaska and the lower 48. We believe that these investments will allow us to offer enterprise customers virtually limitless bandwidth as well as collapsible ring protection designed to

serve their most sensitive interstate data traffic requirements.

4

Table of Contents

In-State Products and Services

We provide a broad array of robust in-state wireline communications services to our residential, business and enterprise customers, including voice, broadband data, network access, long distance and other communications products and services.

Voice services we offer include our local exchange, local private line, wire maintenance, voice messaging and value-added services. Value-added services include caller ID, call waiting, return call and other enhanced telephony features.

Broadband, data and Internet services we offer include MPLS, Metro Ethernet, high-speed and scalable DSL.

Network access services are provided primarily to long distance and other competing carriers who use our local exchange facilities to provide usage services to their customers.

Long distance services we offer include intrastate toll and interstate long distance voice and data services.

Operations

Our wireline segment comprises four lines of business which operate across our subsidiaries and focus on specific customer markets. We are not dependent on any single customer. Our retail line of business provides communications and information services to residential customers and businesses. These services include local and long distance telephone services, including voicemail, caller ID and call forwarding. We also offer retail broadband and Internet services. Our wholesale line of business serves competitive local exchange carriers (CLECs) by offering, for resale, our local exchange network, including unbundled network elements (UNEs). We also offer traditional data services in specific markets, such as private line, frame relay and ATM services, as well as MPLS services. Our network access line of business provides voice and data termination services through our local telephone facilities.

Our enterprise line of business integrates the very best of our voice, data and Internet communications services and targets these combined services to medium and large business customers, multi-national corporations, municipal, state and federal governments, and other telecommunications carriers. Our enterprise line of business relies heavily on our ability to provide redundant high bandwidth data connections throughout Alaska and to the lower 48 states. We seek to provide these customers comprehensive, value-added services that make communications more secure, reliable and efficient.

Competition

The telecommunications industry is highly competitive. Factors contributing to the industry s increasingly competitive market include regulatory changes, product substitution, technological advances, excess network capacity and the entrance of new competitors. In this environment, competition is based on price and pricing plans, the types of services offered, the combination of services into bundled offerings, customer service, the quality and reliability of services provided, and the development of new products and services. Current and potential competitors in telecommunication services include cable companies, wireless service providers, long distance companies, other local telephone companies, foreign telecommunications providers, electric utilities, Internet service providers (ISPs), Internet information providers and other companies that offer network services. Many of these companies have a strong market presence, including national and international presences, brand recognition and existing customer relationships, all of which contribute to intensifying competition and may affect our future revenue growth. For more information associated with the risks of our competitive environment, see Item 1A Risk Factors .

Local Exchange Services

The ability to offer local exchange services has historically been subject to regulation by state regulatory commissions. Applications from competitors to provide and resell local exchange services have been approved in most of our service territory.

We are required to permit competitors to purchase our services for resale, or access components of our network on an unbundled basis at a prescribed cost, and we expect intense competition in our local exchange markets to continue indefinitely. Our telephone operations generally have been required to sell their services to CLECs at significant discounts from the prices we charge our retail customers. The scope of these obligations and the rates we

receive are subject to ongoing review and revision by the Federal Communications Commission (FCC) and the Regulatory Commission of Alaska (RCA). For further information, see the section Regulation below.

Long Distance Services

We offer intrastate toll and interstate long distance services throughout Alaska. The RCA has jurisdiction over intrastate long distance services and the FCC has jurisdiction over interstate long distance services. For further information, see the section Regulation below. A number of our major competitors in the long distance business have strong brand recognition and existing customer relationships, making for a very competitive environment. For further information on our competitive environment, see Item 1A Risk Factors .

Network

We serve approximately 201,000 access lines in Alaska. We continue to upgrade our network in order to provide more customers with broadband capabilities. Our fiber network, which is extensive within Alaska s urban areas and connects the primary areas of Anchorage, Fairbanks and Juneau with each other and the lower 48 states, offers us the opportunity to provide our customers with improved network reliability and speed for voice and data applications. We own and operate the most expansive IP networks in Alaska using MPLS technology. We provide voice, data, and Internet service to all of the major population centers in Alaska.

Following our 2008 acquisition of Crest, we own and operate an undersea fiber system of approximately 1,900 miles with cable landing facilities in Whittier, Juneau, and Valdez, Alaska, and Nedonna Beach, Oregon. Crest s system also includes terrestrial transport components linking Nedonna Beach, Oregon to the Network Operations Control Center in Hillsboro, Oregon and collocation facilities in Portland, Oregon and Seattle, Washington. Further, we expect to invest in the technology and services needed to provide the full range of managed services that enterprise customers expect. In addition, we have nearly completed construction of AKORN, a new state-of-the-art undersea fiber optic cable connecting Alaska with the lower 48 along a diverse path. We expect to commercially deploy AKORN in 2009.

Wireless

Our wireless segment provides facilities-based voice and data services statewide. We operate the largest 3G wireless network in Alaska.

Operations

We provide wireless voice and data services across an extensive statewide 1xRTT CDMA and EVDO Rev A wireless network. In addition, through roaming agreements with major U.S. and Canadian carriers we provide our customers a range of services and coverage throughout the lower 48 states, Hawaii and Canada.

Competition

We face strong competition in our wireless market. Other wireless providers, including other cellular and PCS operators and resellers, serve each of the markets in which we operate. We compete primarily against three other facilities-based wireless service providers: at&t, Inc. (formerly Dobson), General Communications, Inc. (GCI) and Alaska Digitel. During 2008, GCI, our primary wireline competitor and owner of Alaska Digitel, aggressively built out its 3G in-state wireless network. We expect at&t to deploy 3G equipment in Alaska during 2009. GCI also provides GSM based wireless services under its own brand name.

Our pricing structure is competitive with at&t. However, Alaska Digitel and GCI compete heavily on price. Alaska Digitel currently offers many wireless services at prices lower than we do.

We expect competition for both customers and network usage to intensify as a result of the higher penetration levels, the development and deployment of new technologies, the introduction of new wireless and fixed line products and services, new market entrants, the availability of additional spectrum, both licensed and unlicensed and regulatory changes. For example, we face increased competition as a result of the use of other high-speed wireless technologies, such as Wi-Fi and WiMAX, which are being deployed or proposed, to meet the growing customer appetite for wireless communications in fixed, nomadic and fully mobile environments. Additionally, as wireless data proliferates, content is becoming an increasingly significant factor in the appeal of these services. This may give content providers and other participants in the wireless value chain opportunities for increased leverage and/or opportunities to compete for wireless data revenues.

We believe that the following are the most important competitive factors in our industry:

Network reliability, capacity and coverage: Lower prices, improved service quality and new service offerings have led to increased network usage. As a result, the ability to keep pace with network capacity needs

and offer highly reliable coverage through one s own network is important. We have an extensive network, but we continue to look for opportunities to enhance our network and improve coverage and network quality. Our competitors are doing the same.

Pricing: Service and equipment pricing is an important area in which wireless carriers compete. Strong competition has resulted in the marketing of minutes-sharing plans, free mobile-to-mobile calling, and offerings of larger bundles of included minutes or unlimited minutes at fixed price points, with no roaming or long distance charges. We seek to compete in this area by offering our customers services based on the specific needs of Alaskans.

Customer service: Quality customer service is essential to ensure that we can obtain new customers and retain existing customers. We believe that the quality of our customer service is a key factor in retaining our customers and in attracting both new to wireless customers and those customers of other carriers who want to switch their wireless service. Our competitors also recognize the importance of customer service and are focusing on improving the customer experience.

Product Differentiation: As wireless technologies develop and wireless broadband networks proliferate, continued customer and revenue growth will be increasingly dependent on the development of new and differentiated products and services. We are committed to providing customer solutions through the development and rapid deployment of new and innovative products and services.

Sales and Distribution: Key to achieving sales success in the wireless industry is the reach and quality of sales channels and distribution points. We believe that the optimal mix of direct and indirect distribution channels is an important ingredient in achieving industry leading profitability. A goal of our distribution strategy is to increase sales through our company operated stores and our business sales team, as well as through telemarketing and web-based sales and fulfillment capabilities. Supplementing this is an indirect distribution network of retail outlets and prepaid replenishment locations.

Our success will depend on our ability to anticipate and respond to various factors affecting the industry, including the factors described above, as well as new technologies, new business models, changes in customer preferences, regulatory changes, demographic trends, economic conditions, and pricing strategies of competitors. For additional information on these factors, see Item 1A Risk Factors .

Network

A key part of our business strategy is to provide high network reliability. We believe that network reliability is a key differentiator in our market and a driver of customer satisfaction. Consistent with this strategy, we continue to strategically expand and upgrade our network in an effort to provide sufficient capacity and seamless and superior coverage and reliability throughout our licensed area. We conduct systematic drive tests of our network to assess the number of blocked and dropped calls as compared to our competitors, and we market those results. Our network is among the most extensive in Alaska with our network covering approximately 84% of Alaska s population and supporting approximately 150,000 subscribers, as of December 31, 2008. We aim to provide our customers consistent features and high quality service, regardless of location.

Network Technology

Our primary network technology platform, 1xRTT code division multiple access (CDMA), a wireless technology developed by Qualcomm as part of its family of technologies known as CDMA2000, is presently deployed in virtually all of our cell sites. 1xRTT increases the voice traffic capacity available to us and provides increased data speeds. Further, 1xRTT is a modular infrastructure upgrade that has proven to be cost-efficient and practical for rapid deployment. In addition to 1xRTT, in 2004 we began deploying evolution data optimized (EVDO), a 3G, packet-based technology that follows the CDMA2000 technology path. As with 1xRTT, we have been able to implement EVDO, including, most recently, EVDO, Rev. A, by changing and/or adding modular components and software in our network. EVDO and EVDO, Rev. A service, which we brand and market as Mobile Broadband , is available in our major markets and in Alaska s North Slope, which is home to Alaska s largest oil fields. Our competitors are also building out their 3G networks.

Spectrum

We have licenses to provide mobile wireless services on the 800-900 MHz and 1800-1900 MHz portions of the radio spectrum. Collectively, these licenses cover virtually all of Alaska. The 800-900 MHz portion is used to provide

digital cellular voice and data services, while our 1800-1900 MHz portion provides all-digital PCS voice and data services. During 2008, we also acquired a license for Advanced Wireless Spectrum in the 1710-1755/2110-2115 MHZ band from AWS Wireless, Inc.

Services

We believe that increasing the value, features and functionality of our wireless service will help us to retain our existing customers, attract new customers and increase customer usage. Through this approach, we seek to drive further revenue growth in our wireless segment.

We design and market service packages around key customer groups, from the young adult market to enterprise business accounts. We tailor our wireless services, which include both voice and data offerings, and postpaid and prepaid pricing options, to the needs of these customers.

Voice services: We offer a variety of packages for voice services predominantly offered on a postpaid basis with a contract term. Specifically, we offer plans which provide a choice in amounts of bundled minutes or unlimited minutes together with no roaming or long distance charges for calls on our network and the networks of our roaming partners in the rest of the U.S. and Canada; family/small group and shared minute plans for multiple-user households and small businesses; and plans targeted to larger business accounts. We also offer bundled minutes or unlimited minutes plans that target customers needing Alaskan coverage only. Generally, our competitors do the same. In addition, we offer a prepaid product that enables individuals to obtain wireless voice services without a long-term contract by paying in advance.

Data services: We continue to expand our 3G wireless data, messaging and multi-media offerings for both consumer and business customers.

Devices

We offer wireless devices by a number of manufacturers that complement our focus on high quality service and an optimal user experience. Most of the wireless devices that we offer are EVDO-enabled, and all of them are compatible with our 1xRTT network. In addition, the handsets that we offer are headphone/earphone compatible and, all of them, through GPS functionality, are compliant with the FCC s Enhanced 911 (E-911) requirements.

Marketing

Our marketing strategy targets customers needs, promotes our brand, cross markets, and in some cases, bundles our wireline products. Our marketing efforts are focused on a coordinated program of television, print, radio, signage, Internet and point-of-sale media promotions.

Sales and Distribution Channels

Our sales strategy combines direct and indirect distribution channels in order to increase customer growth while reducing customer acquisition costs.

Our company operated stores are a core component of our distribution strategy. Our experience has been that customers entering through this direct channel are generally higher value customers who generate higher revenue per month on average and are less likely to cancel their service than those who come through other mass-market channels. We had 15 company operated stores and kiosks as of December 31, 2008. In addition, our direct channel also includes our business sales organization, which is focused on supporting the needs of larger business customers.

Customer Service, Retention and Satisfaction

We believe that quality customer service increases customer satisfaction, which reduces churn, and is a key differentiator in the wireless industry. We are committed to providing high quality customer service, investing in loyalty and retention efforts and continually monitoring customer satisfaction in all facets of our service.

Seasonality

We believe our wireless revenue is materially impacted by seasonal factors. Wireless revenue, particularly roaming revenue, declines in the winter months and increases in the summer months. We believe this is due to Alaska s northern latitude and the resulting wide swing in available daylight and weather conditions between summer and winter months. These uniquely Alaskan conditions affect business, tourism and calling patterns in the state. Our wireline service offerings experience similar seasonal effects, but we do not believe these effects are material.

Employees

As of January 31, 2009, we employed 967 regular full-time employees, 13 regular part time employees and 2 temporary employees. Approximately 76% of our employees are represented by the International Brotherhood of Electrical Workers, Local 1547 (IBEW). Management considers employee relations to be satisfactory. However, our Master Collective Bargaining Agreement with the IBEW, as amended, that governs the terms and conditions of employment for all IBEW represented employees working for us in the state of Alaska will expire on December 31, 2009. We expect to conduct extensive negotiations with the IBEW during 2009. These negotiations may strain our labor relations and we do not know whether we will complete negotiations on or before the term of our collective

bargaining agreement expires.

Website Access to Reports

Our investor relations website Internet address is www.alsk.com. The information on our website is not incorporated by reference in this annual report on Form 10-K. We make available, free of charge, on our investor relations website, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act. These reports are available as soon as reasonably practicable after we electronically file such material with, or furnish it to, the U.S. Securities and Exchange Commission (SEC).

Regulation

The following summary of the regulatory environment in which our business operates does not describe all present and proposed federal, state and local legislation and regulations affecting the telecommunications industry in Alaska. Some legislation and regulations are currently the subject of judicial review, legislative hearings and administrative proposals, which could change the manner in which this industry operates. We cannot predict the outcome of any of these matters or their potential impact on our business. Regulation in the telecommunications industry is subject to rapid change, and any such change may have an adverse effect on us.

Overview

The telecommunications services we provide and from which we derive a significant share of our revenue are subject to extensive federal, state and local regulation. Our local exchange carrier (LEC) subsidiaries are regulated common carriers and have the right to set maximum rates at a level that allows us to recover the reasonable costs incurred in the provision of regulated telecommunications services and to earn a reasonable rate of return on the investment required to provide these services. Because they face competition, however, most of our LEC subsidiaries may not be able to realize their allowed rates of return.

In this section, Regulation , we refer to our LEC subsidiaries individually as follows:

ACS of Anchorage, Inc. (ACSA);

ACS of Alaska, Inc. (ACSAK);

ACS of Fairbanks, Inc. (ACSF); and

ACS of the Northland, Inc. (ACSN).

In establishing rates for regulated services, our LEC subsidiaries first determine their aggregate costs and then allocate those costs between regulated and non-regulated services, then separate the regulated costs between the state and federal jurisdictions, and finally among their various interstate and intrastate services. This process is governed primarily by the FCC s rules and regulations. The FCC is considering whether to modify or eliminate the current jurisdictional separations process. This decision could indirectly increase or reduce earnings of carriers subject to jurisdictional separations rules by affecting the way regulated costs are divided between the federal and state jurisdictions, if rates in both jurisdictions are not adjusted accordingly. Maximum rates for regulated services are regulated by the FCC for interstate services and by the RCA for intrastate services.

At the federal level, the FCC generally exercises jurisdiction over services of telecommunications common carriers that provide, originate or terminate interstate or international communications and related facilities. The FCC does not directly regulate information services and has preempted inconsistent state regulation of information services. Our wireless services use FCC radio frequency licenses and are subject to various FCC regulations, including E-911 and number portability requirements.

The RCA generally exercises jurisdiction over services and facilities used to provide, originate or terminate communications between points in Alaska. In addition, pursuant to the local competition provisions of the Communications Act of 1934, as amended by the Telecommunications Act of 1996 (Communications Act), federal and state regulators share responsibility for implementing and enforcing certain pro-competitive policies.

Local governments often regulate the public rights-of-way necessary to install and operate networks. These local governments may require communications services providers to obtain licenses or franchises regulating their use of public rights-of-way, and may require carriers to obtain construction permits and abide by building and land use

codes.

Federal regulation

We must comply with the Communications Act and regulations promulgated thereunder, which require, among other things, that communications carriers offer interstate services at just, reasonable and nondiscriminatory rates and terms. The amendments to the Communications Act added provisions intended to promote competition in local telecommunications

services by removing barriers to entry, imposing obligations to offer to competing carriers interconnection and non-discriminatory access to certain facilities and services designated as essential for local competition, and making universal service support explicit and portable, and to lead to deregulation as markets become more competitive.

Interconnection with local telephone companies and access to other facilities

In order to ensure access to local facilities and services at reasonable rates, the Communications Act imposes a number of requirements on LECs. Generally, a LEC must: not prohibit or unreasonably restrict the resale of its services; provide for telephone number portability, so customers may keep the same telephone number if they switch service providers; ensure that customers are able to route their calls to telecommunications service providers without having to dial additional digits; provide access to their poles, ducts, conduits and rights-of-way on a reasonable, non-discriminatory basis; and, when a call originates on its network, compensate other telephone companies for terminating or transporting the call.

Most incumbent LECs (ILECs) have the following additional obligations under the Communications Act: negotiate in good faith with any carrier requesting interconnection; provide interconnection for the transmission and routing of telecommunications at any technically feasible point in its network on just, reasonable and non-discriminatory rates, terms and conditions; provide access to UNEs, such as local loops and trunks, at non-discriminatory, cost-based rates, to competing carriers that would be impaired without them; offer retail local telephone services to resellers at discounted wholesale rates; provide notice of changes in information needed for another carrier to transmit and route services using its facilities; and provide, at rates, terms and conditions that are just, reasonable, and non-discriminatory, physical collocation, which allows a CLEC to install and maintain its network termination equipment in an ILEC s central office, or to obtain functionally equivalent forms of interconnection.

Our ACSN ILEC subsidiary enjoys a statutory exemption as a rural carrier from the requirements imposed on most ILECs to provide UNEs to a CLEC. The RCA may terminate the exemption if it determines that interconnection is technically feasible, not unduly economically burdensome and consistent with universal service. Although the RCA has not terminated ACSN s UNE exemption, the RCA granted GCI, subject to certain conditions, approval to provide local exchange telephone service in the Glacier State study area and Sitka exchange of ACSN on its own facilities. Other than the City of Sitka, all other exchanges in the Sitka study area remain non-competitive at this time. New facilities-based local exchange service competition may reduce our revenues and returns.

To implement the interconnection requirements of the Communications Act, the FCC adopted rules requiring, among other provisions, that ILECs price UNEs based on forward-looking economic costs using the total element, long run incremental cost methodology. In September 2003, the FCC began a reexamination of its pricing standard for UNEs, and may reconsider other aspects of its UNE rules.

On December 28, 2006, the FCC conditionally and partially granted ACSA forbearance from the obligation to lease UNEs to our competitors at regulated rates. This forbearance was limited to five wire centers within the Anchorage service area of ACSA. Even where relief was granted, however, the FCC has required ACS to lease loops and sub-loops at commercially negotiated rates, or if there is no commercial agreement, at the rates for these UNEs in Fairbanks. As a result of this decision, on March 15, 2007, ACSA, ACSAK, ACSF and ACSN entered into a five year global interconnection and resale agreement with GCI governing the provision of UNEs and other services.

Congress may consider legislation that may further modify the interconnection requirements under the Communications Act, and the FCC and the RCA frequently consider modifications of their rules. We cannot predict the outcome of any such action taken by the Congress, the FCC or the RCA.

Interstate access charges

The FCC regulates the prices that ILECs charge for the use of their local telephone facilities in originating or terminating interstate transmissions. Our ILECs interstate access charges are usually developed using a cost-of-service methodology, based on our authorized maximum rate of return. The National Exchange Carrier Association (NECA) develops averaged access rates for participating ILECs, including our ILECs, based on the costs of these carriers. Three of the ACS LECs participate in NECA s tariff for non-traffic sensitive costs, which are primarily loop costs. These same three LECs also participate in NECA s traffic sensitive access tariff which covers primarily switching costs. ACSA no longer participates in the NECA pooling process and has developed and filed its own FCC tariff for

both traffic sensitive and non-traffic sensitive access services. Participants in a NECA tariff charge averaged access rates, pool their revenues, and distribute the revenues on the basis of each individual carrier s costs. The NECA tariffs reduce the cost burden on individual ILECs of filing tariffs and also spread some of the risks of providing interstate access services.

On August 20, 2007, the FCC granted ACSA partial forbearance from certain dominant carrier regulations to ACSA s provision of interstate switched access services, subject to a number of conditions. Among other things, ACSA

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received relief from requirements to base interstate switched access service charges on ACSA s costs plus an authorized rate of return, as well as certain tariffing requirements. The switched access relief was conditioned upon a cap on interstate switched access rates and a cap on USF support received on a per line basis. The FCC denied ACSA s requested similar forbearance relief with respect to interstate special access services. ACSA and other parties have sought reconsideration of the FCC s forbearance order. These reconsideration petitions remain pending.

In October 2008, we filed a petition for waiver of certain FCC rules in order that all of the ACS ILECs interstate prices may be regulated under price-cap regulation rather than rate-of-return regulation, and the ACS ILECs may retain their interstate common line support at the disaggregated per line levels they were receiving in 2008. If the petition is granted, the remaining ACS ILECs would withdraw from the NECA pools, and the traffic sensitive charges of some of the ACS ILECs would likely be lowered over time. ACS has requested that the waivers be granted in time for ACS to file a price-cap tariff effective as of July 1, 2009. at&t and GCI filed comments but neither opposed the petition. The petition remains pending before the FCC.

The FCC is currently considering various proposals for further reform of inter-carrier compensation. Reform proposals now under consideration include a proposed exemption for service providers in Alaska (as well as Hawaii and U.S. Territories), which if adopted could exempt such providers from all or some of any new inter-carrier compensation requirements. The FCC ultimately implements for the rest of the industry. These proposals may result in the elimination of interstate and intrastate access charges paid by long distance carriers, and the requirement that carriers such as ACSA, ACSF, ACSAK and ACSN recover those interstate and intrastate costs from a combination of end-user charges and universal service support. We cannot predict what changes the FCC may adopt or when they may adopt them.

Since 2001, the FCC has been examining aspects of the regulatory framework applicable to interstate special access services provided by price-cap LECs. In particular, the FCC has considered reform of the appropriate rate levels and rate structures for such services; the FCC also has considered whether and to what extent it should retain or modify its special access pricing flexibility rules, pursuant to which price-cap carriers may request authority to provide special access services using more flexible contract tariffs as opposed to standardized tariffs. If the FCC grants the waiver petition discussed above such that ACS becomes a price-cap company, any reforms that the FCC adopts as a part of that ongoing special access proceeding could affect ACS s revenues in ways that we cannot currently predict.

Federal universal service support

The Communications Act requires the FCC to establish a universal service program to ensure that affordable, quality telecommunications services are available to all Americans. The program at the federal level has several components, including one that pays support to LECs serving areas for which the costs of providing basic telephone service are higher than the national average. The Communications Act requires the FCC to make universal service support explicit, expand the types of communications carriers that are required to pay universal support, and allow competitive providers including CLECs and wireless carriers to be eligible for universal service support, including where they serve customers formerly served by ILECs.

USF disbursements may be distributed only to carriers that are designated as eligible telecommunications carriers (ETCs) by a state regulatory commission. All of the ACS ILECs are ETCs in Alaska. In May 2001, the FCC adopted a proposal from the Rural Task Force to reform universal service support for rural areas. As adopted, for an interim period, eligible rural carriers will continue to receive support based on a modified embedded cost mechanism. While the modified embedded cost mechanism remains in place, the FCC has indicated that it will develop a comprehensive plan for high-cost support mechanisms for rural and non-rural carriers which may rely on forward-looking costs.

On May 1, 2008, the FCC adopted an interim, emergency cap on the amount of high-cost support that competitive ETCs may receive, pending the FCC s adoption of comprehensive reform. Such support for each state was capped at the level of support that competitive ETCs (CETCs) were eligible to receive during March 2008 on an annualized basis. The cap became effective on August 1, 2008 and is expected to constrain growth in the total amount of high-cost support available to competitive ETCs.

In its May 1, 2008 Order, the FCC also included an exception from the interim cap for CETCs that serve tribal lands or Alaska Native Regions. All of ACS Wireless, Inc. s service area is located in Alaska Native Regions. CETCs serving those areas may elect to continue to receive uncapped high-cost support for eligible lines except that uncapped support was limited to one payment per each residential account . The ambiguous wording of the exception led to differing interpretations. ACSW, GCI, and Matanuska Telephone Association (MTA) have jointly requested that the FCC clarify that CETCs electing the exception are to receive uncapped support for all eligible lines served in tribal lands and Alaska Native Regions. On March 4, 2009 the FCC adopted an Order granting this request. The practical effect of the Order is to remove the cap on USF support for CETC s on tribal lands and in Alaska.

The FCC is still considering a number of other long-term revisions to the distribution mechanisms for universal service support. The proposals under consideration include eliminating the identical support rule that permits competitive carriers (such as our subsidiary ACS Wireless, Inc. and our wireless competitors) to apply for funding based on the support received by the ILEC. The FCC has proposed requiring competitive carriers to justify support based on some measure of their own costs or on a model. The FCC also has proposed reforms that could affect the amount of funding for ILECs, including using reverse auctions to determine one or more recipients of high-cost support in any geographic area based on the lowest bidder for that support. These potential reforms include a proposed exemption for service providers in Alaska (as well as Hawaii and U.S. Territories), which if adopted could exempt such providers from all or some of any new high-cost support requirements the FCC ultimately implements. These and other proposed rule changes could reduce our support in the future, reduce the support available to our competitors, or provide for new support, such as for broadband services. In addition, members of Congress have indicated that they may seek enactment of legislation addressing universal service reform, including legislation to limit growth of explicit universal service support funds. We are unable to predict whether and to what extent we would be eligible to receive any federal high-cost support under a revised support mechanism.

Under current FCC regulations, the total amount of federal USF available to all ILEC ETCs is subject to a yearly cap. In any year where the cap is reached, the per access line rate at which ILECs can recover USF payments may decrease. In each of the last few years, the cap has effectively decreased USF payments.

Federal universal service contributions

The FCC is currently considering revisions to the current mechanism for funding universal service. Today, our operating subsidiary companies are required to contribute to the federal USF a percentage of their revenue earned from interstate and international services. The FCC is considering whether to replace this funding mechanism with one based on flat-rated, per line contributions, capacity-based contributions, or some combination of these or other proposals. We cannot predict how the outcome of this proceeding may affect our contribution obligations.

Interstate long distance services

FCC regulation of the rates, terms or facilities of our interstate long distance services is relatively light. However, we must comply with the general requirement that our charges and terms be just, reasonable and non-discriminatory. Also, we must comply with FCC rules regarding unauthorized switching of a customer s long distance service provider, or slamming. The FCC has levied substantial fines on some carriers for slamming. In addition, we must post the rates, terms and conditions of its service on our Internet website and engage in other public disclosure activities.

The FCC requires that ILECs that provide interstate long distance services originating from their local exchange service territories must have long distance affiliates which maintain separate books of account and acquire any services from their affiliated ILECs at tariff rates, terms and conditions.

On December 8, 2004, Congress enacted a new law requiring, through 2009, the purchase and sale of interstate wholesale switched service elements at rates equivalent to the rates set forth in AT&T Alascom s Tariff 11, subject to annual downward adjustments specified in the statute. Rural telephone companies, or companies that are affiliated with and under the control of rural telephone companies, are exempt from the requirement to purchase services at such rates.

Broadband and Internet services

We provide broadband Internet access services as an ISP. The FCC has classified such services as information services, so they are not subject to many of the regulatory obligations that are imposed on common carriers. Additionally, the FCC generally has preempted state and local regulation of information services. The FCC has, however, concluded that broadband Internet access providers must comply with the Communications Assistance for Law Enforcement Act (CALEA).

The FCC has imposed particular regulatory obligations on Internet protocol (IP)-based telephony. The FCC has determined that interconnected voice-over-IP (VoIP) providers must comply with: (i) requirements to provide E-911 emergency calling capabilities; (ii) certain disability access requirements; (iii) the FCC s rules protecting customer proprietary network information (CPNI); (iv) local number portability (LNP) requirements; (v) regulatory fee obligations; (vi) obligations under CALEA and (vii) the obligation to contribute to USF.

Additional rules and regulations may be extended to the Internet in the future. A variety of proposals are under consideration in federal and state legislative and regulatory bodies. We cannot predict the outcome or the impact of pending or future proceedings.

Recently, the FCC and lawmakers have considered several proposals to adopt requirements for non-discriminatory treatment of traffic over broadband networks, often referred to as net neutrality . The FCC has released a statement of

12

principles favoring customer choice of content and services available over broadband networks. It also has sought comment on industry practices in connection with this issue and pursued some enforcement action in this area. There may be new legislation or further FCC action to address access to the Internet or create disclosure requirements of ISPs as to treatment of Internet traffic. We cannot predict the impact of any such actions on our results or operations.

In October 2005, the FCC determined that ILECs are no longer required to lease high-speed Internet access service transmission capability to their competitors and re-affirmed its finding that provision of high-speed transmission service bundled with Internet access services is an information service not subject to common carrier regulation, whether that access is provided via cable modem, DSL services or otherwise. This ruling gives us more flexibility in how we offer and price our DSL services. However, for carriers subject to rate-of-return regulation, like the ACS ILECs, the FCC left uncertain whether loop cost allocations would change if they decide to offer the underlying transmission capability on a non-common carrier basis. We currently provide high-speed Internet access transmission capability on a common carrier basis under a stand-alone FCC tariff for ACSA and the NECA tariff for our non-Anchorage LECs. We are considering whether to offer it as non-common carrier service, and if the FCC grants our price cap petition, it may facilitate that decision.

On August 20, 2007, the FCC granted ACSA forbearance from applying common carrier regulation to certain broadband services sold to larger business customers, subject to a condition to develop a plan for allocating costs between rate-of-return regulated services and the non-regulated broadband services. This ruling gives us more flexibility in how we offer and price certain broadband services, and we are considering how to implement this ruling.

Wireless services

The FCC regulates the licensing, construction, operation, acquisition and sale of personal communications services and cellular systems in the United States. All cellular and personal communications services licenses have a 10-year term, at the end of which they must be renewed. Licenses may be revoked for cause and license renewal applications may be denied if the FCC determines that renewal would not serve the public interest. In addition, all personal communications services licensees must satisfy certain coverage requirements. Licensees that fail to meet the coverage requirements may be subject to forfeiture of the license.

Federal law preempts state and local regulation of the entry of, or the rates charged by, any provider of commercial mobile radio services (CMRS) which includes personal communications services and cellular services. The FCC does not regulate such rates; however, the FCC imposes a variety of other regulatory requirements on CMRS operators. For example, CMRS operators must be able to transmit 911 calls from any qualified handset without credit check or validation and are required to provide the location of the 911 caller within an increasingly narrow geographic range. CMRS operators are also required to provide 911 service for individuals with speech and hearing disabilities, or TTY service. Consistent with FCC orders, all new ACSW handset activations have been location-capable since January 1, 2006. Further, ACSW met the FCC s deadline of having 95% of all subscribers using location-capable handsets prior to January 31, 2007.

In March 2008, the U.S. Court of Appeals for the District of Columbia Circuit stayed a November 2007 FCC order requiring that wireless carriers meet E-911 location accuracy standards at a smaller, geographic level, the serving area of the Public Safety Answering Point, that may make compliance more difficult to achieve for some carriers. On July 31, 2008, the FCC asked the Court to remand the case so that it could re-evaluate the rules in response to proposals that it measure E-911 location accuracy compliance at the county level. The FCC then asked for comments on these proposals. We are awaiting further FCC action. Compliance may still be more difficult for smaller and rural carriers even under the revised proposals. We cannot predict the outcome of this proceeding or its impact on ACSW.

The FCC also requires that if a LEC customer wants to retain a telephone number while changing to a CMRS service provider (such as ACSW), the LEC must have the capability to allow this wireline-to-wireless number portability within six months of a bona fide request, where the requesting CMRS carrier s coverage area overlaps the geographic location of the LEC rate center to which the number is assigned unless the LEC can provide specific evidence demonstrating that doing so is not technically feasible. These number portability rules are expected to increase the level of competition among CMRS service providers, but also to increase the ability of CMRS providers to win customers from LECs. This rule has had little impact on our LECs, but we cannot predict the net impact of

these rules on us over the long-term.

Other federal regulations

We are subject to various other federal regulations and statutes, including those concerning the use of CPNI in marketing services. CPNI generally includes information a carrier has regarding the telecommunications services to which its customer subscribes and the customer s use of those services. The FCC limits the ways in which carriers may use or disclose

CPNI and specifies what carriers must do to safeguard CPNI. The FCC has recently adopted amendments to strengthen its rules governing carrier use and disclosure of CPNI.

Other FCC initiatives that may impact our regulated subsidiaries include implementing capabilities pursuant to CALEA to be used by law enforcement officials in executing court authorized electronic surveillance, access to poles, ducts, conduits and rights-of-way, Truth-in-Billing requirements, Equal Employment Opportunity reporting, hearing aid compatibility requirements and anti-slamming rules. We must obtain FCC approval before we transfer control of any of our common carrier subsidiaries or our radio frequency licenses or authorizations, make such an acquisition or discontinue an interstate service. These requirements may impose costs on us and limit our business opportunities.

State regulation

Telecommunication companies are required to obtain certificates of public convenience and necessity from the RCA prior to operating as a public utility in Alaska. The RCA must approve amendments to and transfers of such certificates. In addition, RCA approval is required if an entity acquires a controlling interest in any of our certificated subsidiaries, acquires a controlling interest in another intrastate utility or discontinues an intrastate service. The RCA also regulates rates, terms and conditions for local, intrastate access and intrastate long distance services, supervises the administration of the Alaska Universal Service Fund (AUSF) and decides on ETC status for purposes of the federal USF. Furthermore, pursuant to the Telecommunications Act and the FCC s rules, the RCA decides various aspects of local network interconnection offerings and agreements.

Interconnection

The Telecommunications Act specifies that resale and UNE rates are to be negotiated among the parties subject to approval by the state regulatory commission or, if the parties fail to reach an agreement, arbitrated by the state regulatory commission. The ACS LECs have entered into interconnection agreements with a number of entities including TelAlaska Long Distance, Inc.; GCI; at&t; Alaska DigiTel; Alaska Wireless Communications; Bandwidth.com; Clearwire Telecommunications Services, Inc. and ACSW. In addition, ACSW has entered in to agreements with entities including KPU Telecommunications; Alaska Telephone Company; Arctic Slope Telephone Association Cooperative, Inc.; Matanuska Telephone Association; Mukluk Telephone Company, Inc. and the ACS LECs, to provide service in their study areas.

Competitive local exchange regulations

In August 2005, the RCA adopted regulations addressing a variety of telecommunications related matters including tariff policies, depreciation practices, local competitive market rules and interexchange competitive market rules. The regulations provide for, among other things: initial classification of all ILECs, including our rural properties and ACSA, as dominant carriers; requirements that all carriers, both dominant and non-dominant, offer all retail services for resale at wholesale rates consistent with 47 U.S.C. § 251 and 252; and limited dominant carrier pricing flexibility in competitive areas, under which carriers may reduce retail rates, offer new or repackaged services and implement special contracts for retail service upon 30 days notice. Rate increases affecting existing services are subject to full cost support showings by the dominant carrier in areas with local competition; but the RCA may demand, and has demanded, cost support even for rate reductions and new or repackaged services in competitive areas.

The RCA has defined most of the ACS LEC markets as competitive local exchange markets and designated the ACS LECs as non-dominant carriers in all areas except the rural communities outside the City of Sitka, in the Sitka study area (Sitka Bush). Consequently, non-dominant ACS LECs serving competitive exchanges have access to relaxed tariff filing rules that allow retail offers to be introduced to the market without advance public notice or RCA approval in all areas except Sitka Bush.

End user local rates

The rates charged by our ILECs to end-users for basic local service are generally subject to the RCA s regulation based on a cost-of-service method using an authorized rate of return. Competition may prevent local rates from being sufficient to recover embedded costs for local service. Rate cases are typically infrequent, carrier-initiated and require the carrier to meet substantial burdens of proof. The RCA may, however, investigate, upon complaint or upon its own motion, the rates of a LEC and hold hearings on those rates.

Intrastate access rates

ILECs not yet subject to local competition participate in a pool administered by the Alaska Exchange Carriers Association (AECA) for intrastate access charges to long distance carriers. AECA pools their access costs and sets a statewide average price which participating ILECs charge to long distance carriers for originating or terminating calls. Access revenues are collected in a pool and then redistributed to the ILECs based on their actual costs.

The RCA requires an ILEC to exit the AECA pool and to file separate, individual company access charge tariffs when a competitor enters its service area. These tariffs are based on the ILEC s most recently approved stand-alone revenue requirement. ACSN was our last ILEC to exit AECA. Prior to formal exit, AECA administered ACSN s intrastate access tariff, but ACSN had already implemented a stand-alone rate. In March, 2008, the RCA re-affirmed that it would continue to require ILECs in competitive markets to exit the AECA pool. In June 2008, the RCA accepted ACSN s stipulation allowing it to fully exit the pool. ACSN now operates under a price capped individual access tariff.

Following up on its March 2008 order, the RCA asked for comment on access regulation changes that would shift LECs recovery of access costs from long distance carriers to consumers. The RCA proposed to reduce one long distance carrier access charge and cap LECs monthly access revenues from that charge at $6 per line. To offset lost revenue, the RCA proposed increasing the access fee charged directly to consumers to $4 per line and tapping the state USF, as discussed below. The RCA is no longer considering increasing the customer access charge, but may still reduce the long distance carrier access charge. As another option, the RCA proposed allowing carriers that may be required to leave the State access charge pool to continue to participate in the AECA tariff, but on a stand-alone basis. The order emphasized that the RCA remains open to alternative proposals. The RCA s proposed changes could impact the ACS LECs access revenue levels in ways that we currently cannot predict.

Alaska Universal Service Fund

The RCA has established a state universal service fund, (AUSF). The AUSF serves as a complement to the federal USF, but must meet federal statutory criteria concerning consistency with federal rules and regulations. Currently, the AUSF supports a portion of certain higher cost carriers switching costs, the costs of lifeline service (which supports rates of low income customers), and a portion of the cost of Public Interest Pay Telephones. The RCA has adopted regulations that limit high-cost switching support to local companies with access lines of 20,000 or less. This change has eliminated the switching support that our rural ILECs received.

As part of its intrastate access reform, the RCA is considering whether to provide AUSF support to high-cost, rural LECs to offset access revenue losses. It has also initially proposed expanding the function of the AUSF to support high-cost interexchange facilities of long distance carriers. However, further consideration of interexchange support has been deferred to a future proceeding. Any offsets of reduced access charges would come from the AUSF because the RCA has decided against increasing the customer access charge. Both proposals are designed to reduce pressure on in-state toll rates. It is difficult to predict whether the RCA will move forward on these reforms, particularly since the FCC is considering reforms at the same time that could shift more universal service burden to the states.

ETC Determinations

The RCA granted GCI s request that it be designated an ETC in the Anchorage, Fairbanks, Juneau, Eielson, Fort Wainwright and Glacier State areas, all of which are currently served by our subsidiaries. Further, ACSW has been granted ETC status in the MTA, ACSF, ACSA, ACSAK-Juneau, ACSN-Glacier State, Copper Valley and KPU Telecommunications study areas. On September 11, 2007, the RCA denied ACSW s request for ETC status in the areas served by Alaska Telephone Company and Cordova Telephone Cooperative, Inc., without prejudice to re-filing.

In January, 2008, GCI applied for ETC status in the area served by Mukluk Telephone Company (Nome and surrounding areas) using a hybrid approach incorporating both wireless and fixed wireless (CLEC) technologies. A common carrier designated as an ETC must offer services supported by federal universal service mechanisms throughout the ETC service area either by using its own facilities or a combination of its own facilities and resale of another carrier s services. The RCA rejected GCI s request for a single designation and treated its filing as two separate applications. The RCA granted GCI ETC status for its wireless service but denied it ETC status for its wireline and fixed wireless service. It instructed GCI to request a declaratory ruling from the FCC to resolve unanswered questions regarding the capabilities and appropriate jurisdictional classification of GCI s fixed wireless service. GCI subsequently withdrew its ETC application for fixed wireless. The RCA s ruling could impact the level of universal service funding available to our competitor.

In August 2008, the RCA adopted regulations governing the state process for obtaining and maintaining designation as an ETC that were based in part on the FCC s minimum ETC requirements. The rules added new

requirements for ETCs, including that they will have to strengthen emergency back-up capability, provide detailed plans showing how they will serve the entire service area over time, and file periodic reports showing progress on meeting network development plans for each community. The rules will apply to carriers already designated as ETCs, as well as new ETCs. An ETC may lose its ETC status or USF support if it fails to follow its network build-out and service commitments.

Other state regulations

In 2007, the Commission adopted standards related to E-911 service for multi-line telephones. The rules do not impose any new obligations on local exchange carriers. The owners of the multi-line telephones, such as hotels or motels, will be responsible for changes in their systems, so that 911 callers can be identified more accurately.

Local Service

ACSN serves approximately 200 customers in very remote parts of Alaska through fixed wireless service. Several consumers in two remote southeast locations, South Thorne Bay and Klawock on Prince of Wales Island (PWI), had complained to the RCA about the quality of service provided by the time division multiple access (TDMA) facilities. The RCA opened a docket to formally investigate those complaints and has received similar criticisms from other local customers in the area. Over the last year, ACSN upgraded its fixed wireless service from TDMA to a more advanced CDMA platform. The RCA is planning a hearing to allow ACSN to respond to the consumer complaints, now that its CDMA conversion is complete. The RCA may question ACSN on whether its CDMA upgrade has addressed some of the consumer problems, whether ACSN should extend its wireline network to these customers, and whether its fixed wireless service complies with the State Telecommunications Modernization Plan which requires local companies to meet certain technology standards (*e.g.* data speeds) and other service quality regulations. ACSN had used fixed wireless technology because these customers were in difficult to serve areas. It is not possible to predict the outcome of this proceeding at this time.

Item 1A. Risk Factors

We face a variety of risks that may affect our business, financial condition and results of operations, some of which are beyond our control. The risks described below are not the only ones we face and should be considered in addition to the other cautionary statements and risks described elsewhere, and the other information contained, in this report and in our other filings with the SEC, including our subsequent reports on Forms 10-Q and 8-K. Additional risks and uncertainties not known to us or that we currently deem immaterial may also affect our business. If any of these known or unknown risks or uncertainties actually occurs, our business, financial condition and results of operations could be seriously harmed.

Risks Relating to the Industry in Which We Compete

The telecommunications industry is extremely competitive, particularly in Alaska, and we may have difficulty competing effectively for share in generally small markets.

The telecommunications industry in Alaska is extremely competitive, and providers compete for a small number of customers in small markets. We face competition in each of our wireless and wireline markets. Competitors in our markets:

- reduce our customer base;
- require us to lower rates and other prices in order to compete;
- require us to invest in new facilities and capabilities;
- increase our marketing expenses and require us to use discounting and promotional campaigns that adversely affect our margins; or
- otherwise lead to reduced revenues, margins and returns.

Our principal wireless competitors are at&t, GCI and its subsidiary Alaska Digitel. at&t is one of the largest wireless service providers in the U.S. In addition, at&t has more Alaskan customers than we do. at&t, and to some extent GCI, have greater access to financial, technical and other resources than we do. Further, at&t may have greater access to consumer devices, and greater market power to obtain these devices on more favorable terms, than we do. at&t, thus, might be able to offer lower prices, additional products, services, features or other incentives that we cannot match or offer. GCI and Alaska Digitel compete primarily on price, and their pricing may be perceived as lower than ours. Larger competitors, especially at&t may be in a position to respond more quickly to new technologies and be able to undertake more extensive marketing campaigns. Moreover, at&t operates its own nationwide network,

whereas we rely on roaming agreements with other carriers to provide coverage outside Alaska. Our reliance on these agreements could adversely affect our ability to maintain competitive pricing, which would have a material adverse effect on our financial results.

Our principal wireline competitor is the dominant cable television provider in Alaska. In consumer markets, GCI attempts to use its dominant cable television position by bundling its cable services with competitive telephony services, which are often based on leases of our facilities. We do not offer television service, and, thus, are unable to offer competing bundles. In addition, GCI has aggressively deployed cable telephony in order to move its telephone customers off of our network and onto its own cable system. Significant, continued, migration of customers would result in a significant

reduction of revenue for us. In addition, GCI holds a dominant position in the current long-haul voice and data markets, where it owns and operates two of the three existing undersea fiber optic cables connecting Alaska to the lower 48 and has a number of significant contracts with large carrier customers. GCI competed very aggressively on price in this market during 2008 as it defended its market share. In addition, at&t has acquired a substantial amount of interstate fiber optic capacity from GCI, which may allow it to offer additional competing service from its national platform.

These strong competitive pressures in both our wireless and wireline business segments could have a material adverse effect on our business, operating results, margins and financial condition.

Risks Relating to Our Debt and the Credit Markets

Our substantial debt could adversely affect our financial health, financing options and liquidity position.

We have a substantial amount of debt. As of December 31, 2008, and for the year then ended, we had total long-term obligations, including current portion, of $561.5 million and a loss before income tax benefit of $16.6 million. Our debt could have important consequences for you as a holder of our common stock. For example, our substantial debt could:

- require us to dedicate a substantial portion of our cash flow from operations to payments on our debt, thereby reducing the availability of our cash flow to fund working capital, capital expenditures, future business opportunities, our dividend and other general corporate purposes;
- limit our flexibility to plan, adjust or react to changing economic, market or industry conditions, reduce our ability to withstand competitive pressures, and increase our vulnerability to general adverse economic and industry conditions;
- place us at a competitive disadvantage to many of our competitors who are less leveraged than we are;
- limit our ability to borrow additional amounts for working capital, capital expenditures, future business opportunities, including strategic acquisitions, and other general corporate requirements or hinder us from obtaining such financing on terms favorable to us or at all; or
- limit our ability to refinance our debt.

The terms of our senior credit facility and the terms of our other debt allows us and our subsidiaries to incur additional debt upon the satisfaction of certain conditions. If new debt is added, the related risks described above would intensify.

The downturn in the economy and the volatility in the capital markets could limit our ability to access capital or could increase our costs of capital.

We have seen a dramatic downturn in the U.S. and global economy. The fair value of our long-term debt, as compared to its carrying value, has declined significantly in 2008, primarily due to changes in overall capital market conditions as demonstrated by lower liquidity in the markets, increases in credit spreads, and decreases in bank lending activities, which result in investors moving from high yield securities to lower yield investment grade or U.S. Treasury securities in efforts to preserve capital.

Although we have had continued solid operating cash flow, the downturn and the disruption in the credit markets may reduce sources of liquidity available to us. We can provide no assurance that we will continue to meet our capital requirements from our cash resources, future cash flow and external sources of financing, particularly if current market or economic conditions continue or deteriorate further. We manage cash and cash equivalents in various institutions at levels beyond FDIC coverage limits, and we purchase investments not guaranteed by the FDIC. Accordingly, there may be a risk that we will not recover the full principal of our investments or that their liquidity may be diminished. We rely on multiple financial institutions to provide funding pursuant to existing credit agreements, and those institutions may not be able to meet their obligations to provide funding in a timely manner, or at all, when we require it. The cost of or lack of available credit could impact our ability to develop sufficient liquidity to maintain or grow our business, which in turn may adversely affect our business and results of operations.

Financial covenants in our debt instruments limit our operating flexibility.

Our senior credit facility requires us to maintain certain financial ratios and adhere to other covenants that, among other things, restrict our ability to take specific actions, even if we believe such actions are in our best interest. These include restrictions on our ability to:

- pay dividends or distributions on, redeem or repurchase our capital stock;
- issue certain preferred or redeemable capital stock;
- incur additional debt;

- create liens;
- make certain types of investments, loans, advances or other forms of payments;
- issue, sell or allow distributions on capital stock of specified subsidiaries;
- prepay or defease specified debt;
- enter into transactions with affiliates; or
- merge, consolidate or sell our assets.

A breach of any of these covenants, ratios or tests could result in a default under our senior credit facility. Upon the occurrence of an event of default under our senior credit facility, the lenders could elect to declare all amounts outstanding under our senior credit facility to be immediately due and payable. Such a default or acceleration may allow our other creditors to accelerate our other debt. If the lenders accelerate the payment of the debt under our senior credit facility, our assets may not be sufficient to repay our debts.

We require a significant amount of cash to service our debt, pay dividends, fund our growth projects, and meet other liquidity needs.

Our ability to make payments on and to refinance our debt, including amounts borrowed under our senior credit facility and our 5.75% Convertible Notes due 2013, to pay dividends, and to fund planned capital expenditures, including our AKORN and Northstar long-haul fiber facilities, and any strategic acquisitions we may make, if any, will depend on our ability to generate cash in the future. We cannot assure you that our business will generate sufficient cash flow from operations such that our currently anticipated growth in revenues and cash flow will be realized on schedule or that future borrowings will be available to us in an amount sufficient to enable the repayment of our debt, pay dividends or to fund our other liquidity needs. We may need to refinance all or a portion of our debt, including the senior credit facility, on or before maturity. We may not be able to refinance any of our debt on commercially reasonable terms or at all. If we are unable to refinance our debt or obtain new financing under these circumstances, we would have to consider other options, including:

- sales of certain assets to meet our debt service requirements;
- sales of equity; and
- negotiations with our lenders to restructure the applicable debt.

If we are forced to pursue any of the above options our business and/or the value of our common stock could be adversely affected.

The call options we purchased and the warrants we sold contemporaneously with the sale of our convertible notes may affect the trading price of our common stock and the value of the convertible notes.

The counterparties to the call options we purchased and warrants we sold may engage in hedging activities and modify their hedge positions from time to time prior to the conversion or maturity of our senior convertible notes, particularly around the time of any conversion of the notes. These hedging activities may include purchasing and selling shares of our common stock, or other of our securities, or other instruments, including over-the-counter derivative instruments. The effect, if any, of these activities on the trading price of our common stock or the convertible notes will depend in part on market conditions at the time and cannot be reasonably predicted at this time. Any of these activities could adversely affect the trading price of our common stock and the value of the convertible notes.

Exercise of the outstanding warrants could dilute the ownership interests of our existing stockholders.

Concurrently with the sale of our senior convertible notes, we sold warrants expiring in 2013 to purchase, subject to anti-dilution adjustments, approximately 10.7 million shares of common stock at $16.422. The warrants may not be exercised prior to the maturity of the senior convertible notes due in 2013. The warrants may be settled in

cash at our election. Exercise of the warrants could dilute the ownership interests of our existing stockholders.

Risks related to our Business

We may not successfully complete construction and integration of our AKORN and Northstar fiber facilities that connect Alaska to the Lower 48, and even if we do, we may be unable to operate the combined networks profitably.

Realization of the anticipated benefits of our redundant interstate investments will depend on our ability to successfully integrate them into our businesses and operations and attract significant enterprise customers requiring robust data service capabilities. We will continue to be required to devote significant management attention and resources to sustaining and promoting its operations and maintaining its support. If we fail to properly execute the construction of the fiber facility or if we miss critical deadlines in its implementation or fail to identify critical markets, we could experience serious disruption and harm to our business. We will face challenges to our abilities to do the following:

completing construction of the AKORN facility at an expected total cost of approximately $105 million;

integrating Northstar and other assets acquired from Crest Communications to achieve efficiencies while retaining operational redundancy;

develop attractive products and services that operate seamlessly with our existing technology and infrastructure;

maintain and upgrade timely the complex underlying hardware and software technology that drives optimal use of these facilities;

attract a sufficient volume of traffic on these fiber facilities to make them profitable;

offer products and services that use these fiber facilities that are attractive to our target customers;

preserve key customer, supplier and other important relationships and resolve potential conflicts that may arise; and

generate sufficient revenues to maintain increased indebtedness raised to complete these projects.

If we do not maintain or improve our current relationship with existing customers and develop new large volume and enterprise customers, we may not be able to realize our targets for sales and revenue growth. If we are unable to achieve our projected revenue growth and margins anticipated from the investment, we may be unable to profitably operate these facilities.

Increased supply of interstate and international long-haul fiber in Alaska could adversely impact prices for bandwidth, which could in turn, adversely affect our projected and actual sales, margins and profitability of our fiber facility.

Significant increases in fiber transport capacity in the United States have at times exerted downward pressure on prices, margins and profitability. The market for long-haul fiber in Alaska is characterized by high capital investment and relatively high fixed costs, coupled with a limited number of large customers. Some of our existing and potential competitors have greater name recognition and more established relationships with our target customers. Further, these competitors may have more experience with the repair and maintenance of the underlying data transport technology, and its associated costs, than we do. Our primary wireline competitor, GCI, has adopted a very aggressive pricing policy in the long-haul interstate voice and data markets. GCI has also sold a very large amount of capacity to at&t, which allows them to serve their own needs and sell to others, effectively establishing a national competitor in this market. We cannot predict with any certainty what the prevailing market prices will be for interstate voice and data transport will be or when prices for these services will stabilize, if at all.

We provide services to our customers over access lines and if we continue to lose access lines our revenues, earnings and cash flow from operations may decrease.

Our business generates revenue by delivering voice and data services over access lines. We have experienced net access line loss consistently over the past few years. During the year ended December 31, 2008, the number of access lines we serve declined by 11.0%. We may continue to experience net access line loss in our markets for an unforeseen period of time. Our inability to retain access lines would adversely affect our revenues, earnings and cash flow from operations.

Revenues from access charges may be reduced or lost.

We received approximately 22.7% of our operating revenues for the year ended December 31, 2008 from local exchange network access charges. The amount of revenue that we receive from these access charges is calculated in accordance with requirements set by the FCC and the RCA. Any change in these requirements may reduce our revenues and earnings. Access charges have consistently decreased in past years. We do not receive access revenue related to our competitors retail customers that are served by UNEs or by the competitors own facilities. To the extent

that competitors move customers on to UNEs or off our network entirely, our access revenues will decrease. We do not receive access revenue from VoIP calls, and growth of this service will reduce our access revenues.

The FCC has actively reviewed new mechanisms for inter-carrier compensation that, in some cases, could eliminate access charges entirely. Elimination of access charges would likely have a material adverse effect on our revenue and earnings. In any event, we believe that new mechanisms for inter-carrier compensation would more likely than not reduce this source of revenue. Similarly, the RCA has adopted regulations modifying intrastate access charges that may reduce our revenue.

In addition, we have from time to time been involved in disputes about interstate access revenues. We cannot assure you that claims alleging excess charges will not be made in the future, nor whether we would prevail against such claims.

19

We may not continue to receive as much Universal Service Fund support as we have in the past.

We receive USF (and equivalent state universal service support) revenues, to support our wireline operations in high-cost areas. These federal revenues include universal service support payments for local switching support, interstate common line support or high-cost loop support. High-cost support for our rural and non-rural operations is determined pursuant to different methodologies, aspects of which are now under review. Any changes to the existing rules could reduce the Universal Service Fund revenues we receive. Corresponding changes in state universal service support could likewise have a negative effect on the revenues we receive. We expect total payments from the USF to our rural operations will fluctuate based upon our rural companies average cost per loop compared to the national average cost per loop and are likely to decline based on historical trends. High cost loop support revenue in 2008 totaled $8.7 million.

We also receive USF support for our wireless services in areas where we have been designated an ETC. As an ETC, we receive high-cost universal service support for each wireless line provided in high-cost service areas. Under the current identical support FCC rule CETCs that provide new wireless service in a high-cost service areas, receive the same support as an incumbent ETC. We are a CETC in a number of high-cost areas where we provide wireless services. In a notice of proposed rulemaking adopted on January 29, 2008, the FCC tentatively concluded that the goal of universal service will be better served if the identical support rule for CETCs were eliminated. The FCC also tentatively concluded that CETCs should no longer receive interstate access support (IAS), interstate common line support (ICLS), and local switching support (LSS). The FCC has stated that permitting CETCs to receive IAS or ICLS is inconsistent with how CETCs recover their costs or set rates and that LSS includes a number of assumptions regarding switching costs that are not likely to be accurate for CETCs. The FCC proposed rulemaking would base CETC support instead on a CETCs own costs. In addition, as proposed, new seekers of high-cost support would be required to file cost data demonstrating their costs of providing service in high-cost service areas. CETC revenue in 2008 totaled $18.6 million

We derive a significant portion of our wireless revenue from roaming charges. This revenue may fluctuate or decline in the future as a result of general economic, contractual, and competitive factors.

Approximately 5% of our revenue for the year ended December 31, 2008 was derived from roaming charges incurred by other wireless providers whose customers traveled within our coverage areas. The revenue we recognize from these roaming charges may in the future be volatile or decline as a result of a number of factors, many of which are outside our control. These factors include the strength of the Alaskan economy and its primary industries, including tourism, general economic factors affecting commerce between Alaska and other States and countries, unresolved political matters which may affect public and private spending in Alaska, and others. For example, our service areas include a number of summer tourist destinations in Alaska. As a result, our roaming revenue generally increases during summer months and declines during other periods and depends heavily in these areas on the number of tourists who visit Alaskan tourist destinations. In addition, we cannot assure you our roaming agreements with other providers will continue to generate similar roaming revenues. Our agreements with other carriers have varying terms of varying length, including some which are terminable on short notice. In the event these roaming agreements expire or are terminated, we may be unable to renegotiate or replace these agreements on similar or acceptable terms. Failure to obtain acceptable roaming agreements could lead to a significant decline in our revenue and operating income. Lastly, changes in the network footprints of our roaming partners, or those of our competitors who are able to provide roaming coverage in our service areas, could have a material adverse effect on us.

We have substantial liabilities and cash requirements associated with pension and deferred compensation plans.

Our post-retirement benefits, pension, and deferred compensation plans result in substantial liabilities on our balance sheet. These plans and activities have and will generate substantial cash requirements for us, and these requirements may increase beyond our expectations in future years based on changing market conditions. The difference between plan obligations and assets, or the funded status of the plans, is a significant factor in determining the net periodic benefit costs of our pension plans and the ongoing funding requirements of those plans. Changes in interest rates, mortality rates, health care costs, early retirement rates, investment returns, and the market value of plan assets can affect the funded status of our defined benefit pension, other post-retirement and post-employment benefit plans and cause volatility in the net periodic benefit cost and future funding requirements of the plans. We are

currently reviewing the deficit in plan assets and determining the amount we may be required to pay to maintain adequate funding. Prior to the substantial drawdown in 2008 of the value of plan assets, which occurred solely as a result of the decline in plan asset values, we did not anticipate making any contributions in 2009. This unanticipated increase in pension expense may extend into future years if current market conditions persist. Plan liabilities may impair our liquidity, have an unfavorable impact on our ability to obtain financing, and place us at a competitive disadvantage compared to some of our competitors who do not have such liabilities and cash requirements.

In addition, on behalf of substantially all of our employees, we participate in the Alaska Electrical Pension Fund (the AEPF). The AEPF is a multi-employer pension plan to which we make fixed, per employee contributions though our collective bargaining agreement with the IBEW, which covers our IBEW represented workforce, and a special agreement, which covers most of our non-represented workforce. Because our contribution requirements are fixed, we cannot easily adjust our annual plan contributions to address our own financial circumstances. Further, because we do not control the AEPF, we are not aware at all times whether the plan is fully funded. In general, if a funding shortfall in the AEPF exists, we incur a contingent withdrawal liability. Our contingent withdrawal liability is an amount based on our pro-rata share among AEPF participants of the value of the funding shortfall. This contingent liability becomes due and payable by us if we terminate our participation in the AEPF. Moreover, if another participant in the AEPF goes bankrupt, we would become liable for a pro-rata share of the bankrupt participant s realized, but unpaid, withdrawal liability. This could result in an unexpected contribution requirement which could be substantial, and if it is, making such a contribution would have a material adverse effect on our cash position and other financial results. These sources of potential liability are difficult to predict.

If we do not adapt to technological changes in the telecommunications industry, we could lose customers or market share.

Our success will likely depend on our ability to adapt to rapid technological changes in the telecommunications industry. Our failure to adopt a new technology or our choice of one technology over another may have an adverse effect on our ability to compete or meet the demands of our customers. Technological change could, among other things, reduce the barriers to entry facing our competitors providing local service in our service areas. The pace of technology change and our ability to deploy new technologies may be constrained by insufficient capital and/or the need to generate sufficient cash to make interest payments on our debt and to maintain our dividend policy.

New products and services may arise out of technological developments and our inability to keep pace with these developments may reduce the attractiveness of our services. Some of our competitors may have greater resources to respond to changing technology than we do. If we fail to adapt successfully to technological changes or fail to obtain access to new technologies, we could lose customers and be unable to attract new customers and/or sell new services to our existing customers. We may be unable to successfully deliver new products and services, and we may not generate anticipated revenues from such products or services.

New governmental regulations may impose obligations on us to upgrade our existing technology or adopt new technology that may require additional capital and we may not be able to comply timely with these new regulations.

Our markets are heavily regulated. We cannot predict the extent the government will impose new unfunded mandates on us. Such mandates have included those related to emergency location, providing access to hearing-impaired customers, law enforcement assistance, and LNP. Each of these government mandates has imposed new requirements for capital that we could not have predicted with any precision. Along with these obligations, the FCC has imposed deadlines for compliance with these mandates. We may not be able to provide services that comply with these mandates in time to meet the imposed deadlines. Further, we cannot predict whether other mandates, from the FCC or other regulatory authorities, will occur in the future or the demands they may place on our capital expenditures. For more information on our regulatory environment and the risks it presents to us, see Item 1 Business Regulation .

Union disputes, employee strikes and other labor-related disruptions may adversely affect our operations.

Our collective bargaining agreement with the IBEW expires at the end of 2009. We cannot assure you that future collective bargaining agreements will be on terms in line with our expectations or comparable to agreements entered into by our competitors. Any future agreements may increase our labor costs or strain our relationship with our represented employees. In the meantime, we may make strategic and operational decisions that require the consent of the IBEW. The IBEW may not provide consent when we need it, or it may require additional wages, benefits or other consideration be paid in return for its consent. In the event we are unable to negotiate a mutually satisfactory collective bargaining agreement during 2009, we may experience concerted refusals to work, such as strikes, slow downs, sick outs or other similar activities. These activities would harm our operations and impair our financial performance.

The inability to maintain labor costs at competitive levels could harm our financial performance.

Labor costs are a significant component of our expenses, and approximately 76% of our workforce is represented by the International Brotherhood of Electrical Workers, or IBEW. As a result of our collective bargaining agreement with the IBEW, we may experience pressure to increase wages and benefits for our employees. We believe our labor costs are higher than our competitors who employ a non-unionized workforce. For example, our primary in-state competitor GCI, and its subsidiary Alaska Digitel, do not use union labor and pay lower compensation than we do. We cannot assure you that our labor costs will ever become competitive. In addition, the IBEW has brought and may continue to bring grievances to binding arbitration. The IBEW may also bring court actions and may seek to compel us to engage in the bargaining processes where we believe we have no such obligation. If successful, there is a risk these judicial or arbitral avenues could create additional costs that we did not anticipate.

We depend on key members of our senior management team.

Our success depends largely on the skills, experience and performance of key members of our senior management team, as well as our ability to attract and retain other highly qualified management and technical personnel. There is intense competition for qualified personnel in our industry, and we may not be able to attract and retain the personnel necessary for the development of our business. Our remote location also presents a challenge to us in attracting new senior management talent. If we lose one or more of our key employees, our ability to successfully implement our business plan could be materially adversely affected. We do not maintain any key person insurance on any of our personnel.

We rely on a limited number of key suppliers and vendors for timely supply of equipment and services for our network infrastructure and customer support services. If these suppliers or vendors experience problems or favor our competitors, we could fail to obtain the equipment and services we require to operate our business successfully.

We depend on a limited number of suppliers and vendors for equipment and services for our network and certain customer services. If suppliers of our equipment or providers of services on which we rely experience financial difficulties, service or billing interruptions, patent litigation, or other problems, subscriber growth, and our operating results could suffer. For example, we rely heavily on VeriSign to provide billing services for our wireless segment. In addition, we rely heavily on equipment from Nortel Networks for many of our network elements as well as our redundant lower 48 NOCC. Nortel filed for bankruptcy in January 2009 and we cannot predict the outcome of the bankruptcy proceedings.

Suppliers that use proprietary technology, including CDMA technology, as an integral component of our network, effectively lock us into one or few suppliers for key network components. Other suppliers require us to maintain exclusive relationships under a contract. As a result, we have become reliant upon a limited number of network equipment manufacturers and one wireless billing service provider. In the event it becomes necessary to seek alternative suppliers and vendors, we may be unable to obtain satisfactory replacement suppliers or vendors on economically attractive terms on a timely basis, or at all, which could increase costs and may cause disruption in service.

A failure of our network could cause significant delays or interruptions of service, which could cause us to lose customers.

To be successful, we will need to continue to provide our customers reliable service over our network. In certain important cases our systems lack redundancy or diversity which reduces the reliability of our network. Our network and infrastructure are constantly at risk of physical damage to access lines or other inoperability as a result of human, natural or other factors. These factors may include labor strikes, pandemics, acts of terrorism, sabotage, natural disasters, power surges or outages, software defects, contractor or vendor failures and other disruptions that may be beyond our control. Should we experience a prolonged system failure or a significant service interruption, our customers may choose a different provider and our reputation may be damaged.

A failure of enhanced emergency calling services associated with our network may harm our business.

We provide E-911 service to our customers where such service is available. We also contract from time to time with municipalities to upgrade their public safety answering points such that those facilitates become capable of receiving our transmission of a 911 caller s location information and telephone number. If the emergency call center is unable to process such information, the caller is provided only basic 911 services. In these instances, the emergency

caller may be required to verbally advise the operator of such caller s location at the time of the call. Any inability of the answering point to automatically recognize the caller s location or telephone number whether or not it occurs as a result of our network operations may cause us to incur liability or cause our reputation or financial results to suffer.

Table of Contents

The successful operation and growth of our businesses depends on economic conditions in Alaska.

Substantially all of our customers and operations are located in Alaska. Due to our geographical concentration, the successful operation and growth of our businesses depends on economic conditions in Alaska. The Alaskan economy, in turn, depends upon many factors, including:

- the strength of the natural resources industries, particularly oil production;
- the strength of the Alaskan tourism industry;
- the level of government and military spending; and
- the continued growth of services industries.

The customer base for telecommunications services in Alaska is small and geographically concentrated. According to U.S. Census Bureau estimates, the population of Alaska is approximately 677,000 as of July 1, 2007, approximately 60% of whom live in Anchorage, Fairbanks and Juneau. Alaska s economy is heavily dependent on investment by oil companies and state tax revenues correlate with the price of oil. During 2008, the price of crude oil exhibited significant volatility while declining from $147.00 per barrel in July to nearly $30.00 per barrel in December. We do not know what the long term effect on the Alaskan economy will be or if it will even be stable.

Wireless devices may pose health and safety risks and driving while using a wireless phone may be prohibited; as a result, demand for our services may decrease.

Media reports have suggested that, and studies have been undertaken to determine whether, certain radio frequency emissions from wireless handsets and cell sites may be linked to various health concerns, including cancer. Further, radio frequency emissions may interfere with various electronic medical devices, including hearing aids and pacemakers. If consumers health concerns over radio frequency emission increase, they may be discouraged from using wireless handsets. In addition, studies have indicated that using wireless devices while driving may impair a driver s attention. Regulators may impose or increase restrictions on the location and operation of cell sites or increase regulation on the use of handsets, and wireless providers may be exposed to litigation. New government regulations in these matters may adversely affect our results of operations.

Risks Related to our Common Stock

You may not receive the level of dividends provided for in our dividend policy or any dividends at all.

We are not obligated to pay dividends. Our Board of Directors may decide not to pay dividends at any time and for any reason. We might not generate sufficient cash from operations in the future to pay dividends on our common stock in the intended amounts, or at all. If our cash flows from operations for future periods were to fall below our minimum expectations, we would need either to reduce or eliminate dividends or, to the extent permitted under the terms of our senior credit facility or any future agreement governing our debt, fund a portion of our dividends with borrowings or from other sources. Future dividends, if any, will depend on, among other things, our results of operations, cash requirements, financial condition, contractual restrictions, business opportunities, any competitive or technological developments, our increased need to make capital expenditures, provisions of applicable law, and other factors that our Board of Directors may deem relevant. Should we reduce or eliminate dividends, the market price of our common stock may decline.

Continued volatility in the price of our common stock would negatively affect us and our stockholders.

The trading price of our common stock was extremely volatile during 2008 in response to a number of factors, many of which are beyond our control, including actual or anticipated variations in quarterly financial results, actual or anticipated variations in our dividend policy, changes in financial estimates by securities analysts, and announcements by our competitors of significant acquisitions, strategic partnerships, joint ventures or capital commitments. In addition, our financial results or dividend payments may be below the expectations of securities analysts and investors. Broad market and industry factors have also negatively affected the price of our common stock regardless of our operating performance, and we do not know how long these adverse market conditions will continue. Volatility in our stock price regardless of cause could materially adversely affect the trading market and prices for our common stock, as well as our ability to issue additional securities or to secure additional financing.

Item 1B. Unresolved Staff Comments

None

Item 2. Properties

We own and lease office facilities and related equipment for executive headquarters, administrative personnel, central office buildings, and operations in locations throughout Alaska. Our principal executive and administrative offices are located in Anchorage, Alaska. We believe we have appropriate easements, rights-of-way and other arrangements for the accommodation of our pole lines, underground conduits, aerial, underground and undersea cables and wires, and wireless towers and antennas. However, these properties do not lend themselves to simple description by character and location.

In addition to land and structures, our property consists of equipment necessary for the provision of communication services. This includes central office equipment, customer premises equipment (CPE) and connections, radio and wireless antennas, towers, pole lines, video head-end, remote terminals, aerial, underground and undersea cable and wire facilities, vehicles, furniture and fixtures, computers and other equipment. We also own certain other communications equipment held as inventory for sale or lease.

Substantially all of our assets (including those of our subsidiaries) have been pledged as collateral for our 2005 senior credit facility.

Item 3. Legal Proceedings

We are involved in various claims, legal actions and regulatory proceedings arising in the ordinary course of business, including various legal proceedings involving regulatory matters described under Item 1 Business Regulation . We have recorded litigation reserves of $0.4 million as of December 31, 2008 against certain current claims and legal actions. We believe that the disposition of these matters will not have a material adverse effect on our consolidated financial position, results of operations or cash flows.

The information set forth under Note 19 Commitments and Contingencies in the Notes to Consolidated Financial Statements, included in Part IV, Item 15 of this Report, and is incorporated herein by reference. For an additional discussion of certain risks associated with legal proceedings, see the section entitled Risk Factors in Item 1A of this Report.

Item 4. Submission of Matters to a Vote of Security Holders

No matters were submitted to a vote of security holders during the quarter ended December 31, 2008.

PART II

Item 5. Market for Registrant s Common Equity and Related Stockholder Matters

Our common stock is traded on the NASDAQ Global Select Market under the symbol ALSK . The following table presents, for the periods indicated, the high and low sales prices of our common stock as reported by NASDAQ.

2008 Quarters	High	Low
4th	$12.30	$ 8.05
3rd	$13.90	$10.08
2nd	$12.94	$10.64
1st	$15.18	$11.08

2007 Quarters	High	Low
4th	$16.48	$14.12
3rd	$15.92	$12.60
2nd	$17.15	$14.75
1st	$16.85	$13.40

As of February 20, 2009, there were 43.7 million shares of our common stock issued and outstanding and approximately 402 record holders of our common stock. Because many of our shares of existing common stock are held by brokers and other institutions on behalf of stockholders, we are unable to estimate the total number of stockholders represented by these record holders.

Table of Contents

Dividends

On October 28, 2004, we announced the adoption of a dividend policy by our Board of Directors and declared our first quarterly dividend. The following table summarizes all of the dividends paid from that date forward:

Dividend Number	Announcement Date	Ex-Dividend Date	Record Date	Payment Date	Amount Paid
1	10/28/2004	12/29/2004	12/31/2004	1/19/2005	$0.185
2	3/21/2005	3/29/2005	3/31/2005	4/19/2005	$0.200
3	6/14/2005	6/28/2005	6/30/2005	7/20/2005	$0.200
4	9/16/2005	9/28/2005	9/30/2005	10/19/2005	$0.200
5	11/29/2005	12/28/2005	12/30/2005	1/18/2006	$0.200
6	2/23/2006	3/29/2006	3/31/2006	4/19/2006	$0.215
7	6/21/2006	6/28/2006	6/30/2006	7/19/2006	$0.215
8	9/15/2006	9/27/2006	9/29/2006	10/18/2006	$0.215
9	12/19/2006	12/27/2006	12/29/2006	1/17/2007	$0.215
10	3/21/2007	3/28/2007	3/30/2007	4/18/2007	$0.215
11	6/20/2007	6/27/2007	6/29/2007	7/18/2007	$0.215
12	9/18/2007	9/26/2007	9/28/2007	10/17/2007	$0.215
13	12/17/2007	12/27/2007	12/31/2007	1/17/2008	$0.215
14	3/14/2008	3/27/2008	3/31/2008	4/16/2008	$0.215
15	6/13/2008	6/26/2008	6/30/2008	7/16/2008	$0.215
16	9/15/2008	9/26/2008	9/30/2008	10/15/2008	$0.215
17	12/16/2008	12/29/2008	12/31/2008	1/21/2009	$0.215

Based on approximately 43.7 million shares outstanding on February 20, 2009,and an assumed dividend of $0.86 per share, per annum, dividends payable during 2009 would be approximately $37.6 million.

Our ability to make dividend payments in the future will depend on future economic conditions and on financial, business, regulatory and other factors, many of which are beyond our control. Accordingly, our Board of Directors may modify or revoke this policy at any time. Thus, you may not receive any dividends.

Factors that may affect our dividend policy are:

- we are a holding company and rely on dividends, interest and other payments, advances and transfer of funds from our subsidiaries to meet our debt service and pay dividends;

- we may not have enough cash to pay dividends due to changes in our operating earnings, working capital requirements and anticipated cash needs;

- nothing requires us to declare or pay dividends;

- while the dividend policy adopted by our Board of Directors reflects an intention to distribute a substantial portion of our cash generated by our business in excess of operating needs, interest and principal payments on debt and capital expenditures; to pay dividends, our board could modify or revoke this policy at any time;

- even if our dividend policy is not modified or revoked, the actual amount of dividends distributed under the policy and the decision to make any distribution will remain, at all times, entirely at the discretion of our Board of Directors;

- the amount of dividends that we may distribute will be limited by restricted payment and leverage covenants in our 2005 senior credit facility, and potentially, the terms of any future debt that we may incur;

the amount of dividends that we may distribute is subject to restrictions under Delaware law; and

our stockholders have no contractual or other legal right to dividends.

See Item 1A Risk Factors Risks related to our Common Stock . You may not receive the level of dividends provided for in our dividend policy or any dividends at all.

Table of Contents

Securities Authorized for Issuance under Equity Compensation Plans

The information set forth in this Report under Item 12 Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters Securities Authorized for Issuance under Equity Compensation Plans is incorporated herein by reference. For additional information on our stock incentive plans and activity, see Note 15 Stock Incentive Plans in the Notes to Consolidated Financial Statements , included in Part IV, Item 15 of this Report.

Item 6. Selected Financial Data

Selected Historical Financial Data

The following selected consolidated financial data should be read in conjunction with our Consolidated Financial Statements and the Notes thereto in Part II, Item 8 and Management s Discussion and Analysis of Financial Condition and Results of Operations in Part II, Item 7 of this report. We derived the selected consolidated financial data as of December 31, 2008, 2007, 2006, 2005 and 2004 and for the years ended December 31, 2008, 2007, 2006, 2005 and 2004 from our audited consolidated financial statements, and accompanying notes, included in Part II, Item 8 of this report.

($ in thousands)	2008	2007	2006	2005	2004
Operating Data:					
Operating revenues	$389,597	$385,785	$348,721	$326,809	$302,707
Net income (loss)	(10,139)	144,136	13,278	(41,635)	(39,294)
Income (loss) per share basic	$ (0.23)	$ 3.38	$ 0.32	$ (1.04)	$ (1.33)
Income (loss) per share diluted	$ (0.23)	$ 3.26	$ 0.31	$ (1.04)	$ (1.33)
Cash dividends per share	$ 0.86	$ 0.86	$ 0.86	$ 0.80	$ 0.19
Balance Sheet Data (end of period):					
Total assets	$757,338	$663,203	$556,216	$576,413	$637,127
Long-term debt, including current portion	561,523	432,996	438,213	445,578	525,889

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis should be read in conjunction with the consolidated financial statements and related notes and the other financial information included elsewhere in this Form 10-K.

Overview

We believe we are the leading provider of integrated communications services in Alaska. Our wireline business comprises one of the most expansive end-to-end IP networks in Alaska and the largest local exchange carrier network in Alaska. We believe our wireless business comprises the most extensive, reliable wireless network in Alaska with the largest 3G coverage. For more information on our business, services, and products, see Item 1 Business in Part I this Form 10-K.

The sections that follow provide information about important aspects of our operations and investments and include discussions of our results of operations, financial condition and sources and uses of cash. In addition, we have highlighted key trends and uncertainties to the extent practicable. The content and organization of the financial and non-financial data presented in these sections are consistent with information we use in evaluating performance and allocating resources. We also monitor the state of the economy in general. In doing so, we compare Alaskan economic activity with broader economic conditions. In general, we believe that the Alaskan telecommunications market, as well as general economic activity in Alaska, is affected by certain economic factors, which include:

- activity in the oil and gas markets;
- military activity;
- the cost of long-haul telecommunications bandwidth;

local customer preferences;

average usage of Internet technology;

unemployment levels; and

housing activity.

We have observed variances in economic effect on Alaska when compared to the U.S. as a whole. Some factors, particularly, the price of oil and gas, may have the opposite effect on the Alaskan economy than they may have on the U.S. economy as a whole. In forecasting the local economic conditions that affect us, we take particular note of these factors.

Our results of operations, financial position and sources and uses of cash in the current and future periods reflect our focus on the following strategic imperatives:

Emphasis on Top-Line Growth: We emphasize revenue growth as well as growth in net cash provided by operating activities. We devote more resources to higher growth markets such as wireless, including wireless data, wireline broadband connections, including our long-haul fiber optic cables connecting our network to the lower 48, as well as expanded strategic services to business markets, rather than to the traditional wireline voice market.

Investment with Discipline: We focus on gaining market share in those markets that contain high revenue producing customers. In our wireline business, we focus on deploying and selling broadband connections in each market covered by our network. We have targeted investment in deploying high-speed fiber conductivity in and between Alaska s urban centers. During 2008, we invested heavily in interstate capacity through our purchase of Crest Communications and construction of AKORN. We have increasingly targeted carrier and enterprise customers. Revenues from these customers grew 42.9% compared with last year, primarily driven by sales of advanced IP services and increases in revenues from agreements with carriers to terminate their Alaskan long distance traffic. We have directed resources towards offering wireless plans that encourage customer adoption of large monthly-minute postpaid plans and unlimited postpaid plans. By directing resources carefully, we seek to distinguish ourselves from our competitors in a cost effective way.

Process Improvement: While focusing resources on revenue growth and market share gains, we continually challenge our management team and employees at all levels to lower expenses and improve the customer experience through process improvements. We expect to invest in technology-assisted process improvement, including self-service initiatives. We expect efforts such as call center routing improvements, deploying self-pay kiosks and customer service tools to improve our cost structure and maintain or improve operating income margins. As a result of past successes, we have been able to serve more customers while maintaining our workforce at or below prior levels.

Pay for Performance: We embrace a culture of urgency and accountability. We establish goals for all of our employees that are tied to the imperatives described above. We seek to provide our non-represented employees cash incentives and equity compensation that are tied to these goals. We design executive compensation programs carefully to align executives and shareholders long-term interests.

We aim to create value for our shareholders by carefully investing cash flows generated by the business in specific opportunities and transactions that support these imperatives. In addition, we use our cash flows to maintain and grow our dividend payout to shareholders. In light of continued uncertainty in the U.S. credit markets, our Board of Directors has continued to maintain our current $0.86 per share annual dividend policy. Under this policy, the company returned approximately $37.3 million in cash dividends to our stockholders during 2008.

Recent Acquisition

On October 30, 2008, we closed on the purchase of 100% of the outstanding stock of Crest Communications Corporation. The results of Crest s operations have been included in our Wireline segment in the Consolidated Financial Statements since that date. Crest s operations include an undersea fiber system of approximately 1,900 miles with cable landing facilities in Whittier, Juneau, and Valdez, Alaska and Nedonna Beach, Oregon. The system also includes terrestrial transport components linking Nedonna Beach, Oregon to the Network Operations Control Center in Hillsboro, Oregon and collocation facilities in Portland, Oregon and Seattle, Washington. We believe that the acquisition will complement our AKORN fiber build, by providing meaningful operating efficiencies and cost synergies, by offering enterprise customers the only diverse and redundant routing of traffic between Alaska and the lower 48, by allowing management the use of Network Operations Control Centers in Alaska and the lower 48, and by

connecting our network to Southeast Alaska. Furthermore, we believes that the acquisition will drive incremental utilization of our differentiated Alaskan terrestrial assets from Crest s customer base and allow us to participate in the fast-growing bandwidth market ahead of AKORN s commercial launch.

A valuation of the business enterprise and acquired assets and liabilities was performed resulting in a determination that the fair value of the business enterprise was greater than the total acquisition price. The major asset acquired was the Northstar fiber network connecting Alaska with the lower 48, which was valued at replacement cost. These costs were derived from our current build out of the AKORN fiber. In accordance with SFAS No. 141-
Business

Table of Contents

Combinations (SFAS 141), the total cost of the acquisition has been allocated to the assets acquired and the liabilities assumed based on a pro-rata reduction of their estimated fair value at the date of acquisition. Certain purchase price adjustments are still under review and therefore the purchase price allocation is still subject to refinement.

The aggregate purchase price was $65.0 million, net of $1.1 million in cash acquired and inclusive of $4.2 million of cash consideration that has been placed in an escrow account for the settlement of any potential claims of misrepresentations, breach of warranties or covenants or for other indemnifications during the first eighteen months following the closing. The Company and Crest have made customary representations and warranties and covenants in the Agreement. Additionally, $4.0 million has been deferred from the purchase price and placed in an escrow account, until a specific claim for an unapproved asset sale has been resolved.

Revenue Sources by Segment

Wireline

Revenue from our wireline business services is generated from retail, wholesale and enterprise customer segments as well as from the provision of network access services to interexchange and wireless carriers.

Our Retail Business:

We generate revenue from retail residential and business customers primarily from:

- basic local telephone service including features to customers within our service areas;
- ISP services including DSL and dial up;
- long distance services;
- space and power services to business customers; and
- CPE sales to business customers.

The number of local telephone customers we serve continues to steadily decline. We expect this trend to continue.

The table below sets forth subscriber numbers as of December 31, 2008, 2007 and 2006:

	As of December 31		
	2008	2007	2006
Local telephone	174,524	185,658	194,815
Annual growth rate	*-6.0%*	*-4.7%*	*-2.3%*
DSL	47,648	47,501	44,066
Annual growth rate	*0.3%*	*7.8%*	*22.9%*
Dial up	6,741	9,125	12,591
Annual growth rate	*-26.1%*	*-27.5%*	*-27.6%*
Long distance	64,252	65,256	63,995
Annual growth rate	*-1.5%*	*2.0%*	*13.6%*

Our Wholesale Business:

We generate revenue from wholesale customers primarily from:

- providing competitive local service to CLECs on either a wholesale or UNE basis as prescribed under the Telecommunications Act;
- carrier billing and collection services; and
- providing carriers with access to space and power at our central office locations.

The number of telephone lines we serve on a wholesale basis has continued to decline. The rate of wholesale line loss has outpaced the rate of retail line loss generally and has accelerated since 2005. This accelerated decline is primarily a result of a specific CLEC customer migrating its customers onto its own cable telephony plant. The table

below sets forth subscriber numbers as of December 31, 2008, 2007 and 2006:

	As of December 31		
	2008	2007	2006
UNE and resale local	26,844	40,696	57,852
Annual growth rate	*-34.0%*	*-29.7%*	*-19.1%*

28

Our Enterprise Business:

We generate enterprise revenue from large business customers, state and federal governments, and other carriers primarily from local and long distance private line services;

provision of virtual network facilities to nationwide carriers for long distance voice termination;

advanced network services; and

capacity sales on our in-state terrestrial fiber facility.

Our Network Access Business:

Our LECs provide access service to numerous interexchange carriers and may also bill and collect long distance charges from interexchange carrier customers on behalf of the interexchange carriers. The amount of access charge revenue associated with a particular interexchange carrier varies depending on long distance calling patterns and the relative market share of each long distance carrier. The major sources of network access revenue are:

interstate access charges;

intrastate access charges;

federal USF support; and

wireless carrier access charges.

Wireless

Our business provides wireless voice and data services, other value-added services across our owned and operated network in Alaska and across the lower 48 states, Hawaii and Canada with our roaming partners. We generate wireless revenue primarily from:

sale of pre-paid and post-paid wireless voice plans to our Alaskan subscribers;

sale of value-added feature services, including data, to our Alaskan subscribers;

equipment sales;

providing lower 48 and Canadian carriers with roaming access to our network for their subscribers; and

CETC subsidies.

Our wireless business has been a principal driver of revenue growth since 2005. However, as competition increases and markets become increasingly penetrated, we expect that the pace of growth in the future will not reflect our past experience. The table below sets forth subscriber numbers as of December 31, 2008, 2007 and 2006:

	As of December 31		
	2008	2007	2006
Retail wireless	149,466	144,449	130,971
Annual growth rate	*3.5%*	*10.3%*	*16.1%*
Wholesale wireless	346	1,999	3,017
Annual growth rate	*-82.7%*	*-33.7%*	*-35.6%*

Table of Contents

Results of Operations

The following table summarizes our company s operations for the years ended December 31, 2008, 2007, and 2006. Net income for the year ended December 31, 2008 was affected by a one-time impairment charge on goodwill and intangible assets of $29.6 million. Net income for the year ended December 31, 2007 was affected substantially by a one-time, non-cash income tax benefit resulting in a net benefit of $111.2 million arising out of the full release of a reserve previously held against our deferred tax asset.

($ in thousands, except per share data)	2008	2007	2006
Operating revenues:			
Wireline	$ 246,028	$ 248,265	$ 233,351
Wireless	143,569	137,520	115,370
Total operating revenues	389,597	385,785	348,721
Operating expenses:			
Wireline (exclusive of depreciation and amortization)	185,321	179,456	172,421
Wireless (exclusive of depreciation and amortization)	84,751	74,305	62,478
Depreciation and amortization	74,002	71,337	69,096
Loss on disposal of assets, net	750	248	1,105
Loss on impairment of goodwill and intangible assets	29,641		
Total operating expenses	374,465	325,346	305,100
Operating income	15,132	60,439	43,621
Other income and expense:			
Interest expense and loss on extinguishment of debt	(32,921)	(28,741)	(40,095)
Interest income and other	1,148	1,244	10,195
Total other income (expense)	(31,773)	(27,497)	(29,900)
Income (loss) before income taxes	(16,641)	32,942	13,721
Income tax benefit (expense)	6,502	111,194	(443)
Net income (loss)	$ (10,139)	$ 144,136	$ 13,278
Net Income (loss) per share:			
Basic	$ (0.23)	$ 3.38	$ 0.32
Diluted	$ (0.23)	$ 3.26	$ 0.31
Weighted average shares outstanding:			

Basic	43,391	42,701	42,045
Diluted	43,391	44,185	43,387

Table of Contents

Year ended December 31, 2008 Compared to the Year ended December 31, 2007

Wireline

The following table summarizes wireline revenue by source for the years ended December 31, 2008, 2007 and 2006.

	Year Ended December 31,				
	2008		2007		2006
	Amount	Change	Amount	Change	Amount
Wireline Revenue by Source:					
Retail	$ 94.7	-3.3%	$ 97.9	2.4%	$ 95.6
Wholesale	20.4	-13.6%	23.6	-7.1%	25.4
Access	93.9	-6.9%	100.9	6.8%	94.5
Enterprise	37.0	42.9%	25.9	44.7%	17.9
	$ 246.0	-0.9%	$ 248.3	6.4%	$ 233.4

Operating Revenues

Retail: Retail revenue decreased by $3.2 million, or 3.3% in 2008. The decrease was driven by a $2.9 million decline in local exchange revenue primarily associated with residential line losses, a $0.9 million decline in long distance sales, $0.3 million in lower CPE sales to businesses, and a $0.6 million decrease in dial up ISP revenue. These losses were offset, in part, by a $1.7 million increase in revenue from our DSL subscriber base.

Declines in retail switched access lines in service of 6.0% in 2008 were concentrated in the residential market and were driven by wireless substitution and competition.

Wholesale: Wholesale revenues decreased by $3.2 million, or 13.6%, in 2008 due to declines in UNE and wholesale local revenue which is primarily attributable to the ongoing migration of lines leased to our key competitor to cable telephony, offset in part by a negotiated increase in rates. These losses were partially offset by higher revenues from billing and collection, and space and power services.

Total UNE and wholesale lines declined by 34.0% in 2008, to 26,844, as a result of the ongoing migration of lines over to cable telephony. As a result of ongoing declines in UNE and wholesale local lines, we expect that wholesale revenue will decline as a component of wireline revenue for the foreseeable future.

Network Access: Network access revenues decreased by $7.0 million, or 6.9% in 2008. In 2008 and 2007, we benefited from a $6.3 million and $10.1 million, respectively, in net out of period settlements and net reserve releases. The 2008 out of period revenue included a $5.5 million reserve release primarily related to refundable USF support while the 2007 settlement included $5.4 million in settlements with NECA and Universal Service Administrative Company (USAC) for our cost studies. In addition, high-cost loop support decreased by $2.7 million and intrastate revenue decreased by $1.7 million due to lower demand driven, in part, by the continued shift of voice traffic to wireless networks. We expect network access revenue to decline as a component of revenue for the foreseeable future.

Enterprise: Enterprise revenue increased by $11.1 million, or 42.9%, in 2008 due to $7.5 million in revenue from the provision of virtual network facilities to lower 48 carriers for long distance voice termination, $1.5 million from higher sales of advanced network services to large business and government customers, $0.9 million from a capacity exchange agreement with another carrier and an increase of $0.8 million in point-to-point private line services.

Wireless

Wireless revenue increased $6.1 million, or 4.4%, to $143.6 million for the year ended December 31, 2008 compared to $137.5 million for the year ended December 31, 2007. This increase is due primarily to the following:

- growth in average subscribers of 5.1% to 148,114 from 140,863 for the year ended December 31, 2008 and 2007, respectively;

higher phone and accessory sales in the year ended December 31, 2008 resulting in $11.1 million of handset revenue compared to $9.3 million for the year ended December 31, 2007; and

higher revenue from non-ACS customers roaming on our network resulting in third party roaming revenue increasing to $20.5 million from $18.1 million for the year ended December 31, 2008 and 2007, respectively.

Table of Contents

Offsetting these gains was a decrease in average revenue per unit (ARPU) of 2.5% to $61.01 from $62.58 for the year ended December 31, 2008 and 2007, respectively, following proactive measures taken to match national pricing points for voice plans.

Operating Expense

Operating expense increased $49.1 million, or 15.1%, to $374.5 million for the year ended December 31, 2008, from $325.3 million for the year ended December 31, 2007. Depreciation and amortization associated with the operation of each of our segments has been included in total depreciation and amortization.

Wireline: Wireline expenses, which include local telephone, Internet and interexchange operating costs increased $5.9 million, or 3.3%, for the year ended December 31, 2008. The increase is primarily attributable to a $4.8 million increase in LD interstate COGS, $3.5 million in start up costs for our strategic long haul fiber investments, a $1.1 million increase in outside services and consulting costs, a $0.9 million increase in ISP access and circuit expenses, a $0.5 increase in utility costs, and a $1.8 million non-recurring expense benefit in the prior year due to a favorable settlement on a long-term property tax dispute. Offsetting these increases were declines of $3.4 million in labor, $1.3 million in an affiliate B&C charges, $1.6 million in DSL COGS and $0.6 million in lower advertising costs associated with our DSL service.

Wireless: Wireless expense increased $10.4 million, or 14.1%, for the year ended December 31, 2008 compared to the year ended December 31, 2007. The increase is primarily attributable to an increase of $3.7 million in handset, accessory and data content expense, $3.4 million in costs associated with backhaul for our expanded wireless footprint, a $2.4 million increase in employee sales and service costs and a $0.4 million increase in regulatory surcharges.

Depreciation and Amortization: Depreciation and amortization expense increased $2.7 million, or 3.7%, for the year ended December 31, 2008 compared to the year ended December 31, 2007. The change is due to an increase in depreciable asset base partially offset by a number of asset classes reaching their maximum depreciable lives.

Loss on Impairment of Goodwill and Intangible Assets: In the fourth quarter of 2008 we determined that $29.6 million of goodwill and intangibles were impaired on our wireline segment. The goodwill impairment charge is primarily driven by adverse equity market conditions, the industry transition from wireline to wireless products and services, decreases in current market multiples and the decline in our stock price throughout 2008. This non-cash charge reduces goodwill, but does not impact our overall business operations or cash flows. The tax benefit derived from recording the impairment charge was recorded as a deferred income tax benefit and is included in the deferred tax assets as part of our net operating loss carry forwards.

Other Income and Expense: Other income and expense was a net expense of $31.8 million in the year ended December 31, 2008, an increase of 15.6% from the $27.5 million in the year ended December 31, 2007. The increase is primarily attributable to the increase in interest expense in 2008 associated with our new 5.75% convertible debt instrument.

Income Taxes: In the year ended December 31, 2008, we recorded a tax benefit of $6.5 million related to the build up of deferred tax assets from our $16.6 million book loss. In the year ended December 31, 2007, we recorded a net benefit of $111.2 million when we reversed 100% of our valuation allowance. We released the reserve as we believed it was more likely than not, that all of the deferred tax assets would be realized based on the weight of all available evidence, including two years of positive net income and our projected earnings. In 2008, if it were not for the bonus depreciation taken for tax purposes allowed under the Economic Stimulus Act of 2008 , we would have recorded income for tax purposes.

Net Income (loss): Net income decreased to a loss of $10.1 million in 2008, from income of $144.1 million in 2007. The change is primarily the result of incurring a goodwill impairment charge of $29.6 million assessed against our wireline segment in 2008, while 2007 benefited from the one-time reversal of the $122.5 million valuation allowance for our deferred tax asset.

Table of Contents

Year ended December 31, 2007 Compared to the Year ended December 31, 2006

Wireline

The following table summarizes wireline revenue by source for the years ended December 31, 2007, 2006 and 2005.

	Year Ended December 31,				
	2007		2006		2005
	Amount	Change	Amount	Change	Amount
Wireline Revenue by Source:					
Retail	$ 97.9	2.4%	$ 95.6	-2.6%	$ 98.2
Wholesale	23.6	-7.1%	25.4	-19.4%	31.5
Access	100.9	6.8%	94.5	-0.9%	95.4
Enterprise	25.9	44.7%	17.9	15.5%	15.5
	$ 248.3	6.4%	$ 233.4	-3.0%	$ 240.6

Operating Revenues

Retail: Retail revenue increased by $2.3 million, or 2.4% in 2007. The increase was primarily driven by growth in revenue from our DSL subscriber base of $1.6 million and a $1.2 million increase in long distance sales. These gains were offset in part by a $0.6 million decline in local exchange revenue primarily associated with residential line losses; and a $0.7 million decline in dial up ISP revenue.

Declines in retail switched access lines in service of 4.7% in 2007 were concentrated in the residential market and were driven by wireless substitution and competition. During 2007 we added 3,400 DSL connections and exited the year with 47,500 DSL subscribers.

Wholesale: Wholesale revenues decreased by $1.8 million, or 7.1%, in 2007 due to declines in UNE and wholesale local revenue of $2.9 million which is primarily attributable to the ongoing migration of lines leased to our key competitor to cable telephony, offset in part by a negotiated increase in rates. These losses were partially offset by higher revenues from billing and collection, and space and power services.

Total UNE and wholesale lines declined by 29.7% in 2007, to 40,696, as a result of the ongoing migration of lines over to cable telephony. As a result of ongoing declines in UNE and wholesale local lines, we expect that wholesale revenue will decline as a component of wireline revenue for the foreseeable future.

Network Access: Network access revenues increased by $6.4 million, or 6.8% in 2007. This revenue increase is counter to longer term trends where we foresee network access revenue declining as a component of wireline revenue, and was primarily attributable to positive settlements of $4.5 million with NECA and $2.0 million with USAC regarding our cost studies.

Enterprise: Enterprise revenue increased by $8.0 million, or 44.7%, in 2007 due to $3.0 million in revenue from the provision of virtual network facilities to lower 48 carriers for long distance voice termination; $2.4 million from a capacity exchange agreement with another carrier; $1.5 million from higher sales of advanced network services to large business and government customers; and an incremental $1.0 million of capacity sales on our terrestrial fiber.

Wireless

Wireless revenue increased $22.2 million, or 19.2%, to $137.5 million for the year ended December 31, 2007 compared to $115.4 million for the year ended December 31, 2006. This increase is due primarily to the following:

- growth in average subscribers of 13.1% to 140,863 from 124,591 for the year ended December 31, 2007 and 2006, respectively;

- an increase in average ARPU of 6.6% to $62.58 from $58.71 for the year ended December 31, 2007 and 2006, respectively, primarily as a result of increased plan revenue, feature revenue, wireless data revenue, roaming revenue, regulatory surcharges and receipt of CETC funding which added $10.69 and $9.49 to

wireless ARPU for the year ended December 31, 2007 and 2006, respectively;

higher phone and accessory sales in the year ended December 31, 2007 resulting in $9.3 million of handset revenue compared to $8.2 million for the year ended December 31, 2006; and

higher revenue from non-ACS customers roaming on our network resulting in third party roaming revenue increasing to $18.1 million from $14.2 million for the year ended December 31, 2007 and 2006, respectively.

Operating Expense

Operating expense increased $20.2 million, or 6.6%, to $325.3 million for the year ended December 31, 2007, from $305.1 million for the year ended December 31, 2006. Depreciation and amortization associated with the operation of each of our segments has been included in total depreciation and amortization.

Wireline: Wireline expenses, which include local telephone, Internet and interexchange operating costs increased $7.0 million, or 4.1%, for the year ended December 31, 2007. The increase is primarily attributable to activity supporting our Internet service offerings including $3.1 million in ISP access and circuit expense and $1.2 million in DSL COGS. Additionally, we saw a $1.5 million increase in advertising expenses, and a $1.7 million increase in expenses associated with large CPE contracts. These expenses were partially offset by $1.0 million in net non-recurring expense benefits comprising $1.8 million from a favorable settlement of a long-term property tax dispute and $0.8 million in contingent liability charges for an anticipated loss on a vendor agreement.

Wireless: Wireless expense increased $11.8 million, or 18.9%, for the year ended December 31, 2007 compared to the year ended December 31, 2006. The increase is primarily attributable to $7.2 million in costs associated with expanding our wireless footprint, an increase of $2.0 million in handset and accessory and data content expense and a $2.3 million increase in employee sales and service costs to support our growing customer base.

Depreciation and Amortization: Depreciation and amortization expense increased $2.2 million, or 3.2%, for the year ended December 31, 2007 compared to the year ended December 31, 2006. The change is due to an increase in depreciable asset base partially offset by a number of asset classes reaching their maximum depreciable lives. In addition, we recorded additional depreciation expense and a corresponding reduction of our regulatory asset of $5.2 million for the twelve months ended December 31, 2007.

Loss on Disposal of Assets: The loss on disposal of assets decreased year over year $0.9 million from December 31, 2006, due to higher retirements in the prior year arising from our process improvement initiatives.

Other Income and Expense: Other income and expense was a net expense of $27.5 million in the year ended December 31, 2007, a decrease of 8.0% from the $29.9 million in the year ended December 31, 2006. The decline is primarily attributable to a number of large prior year non-recurring transactions. These transactions included a $9.6 million loss on the extinguishment of debt, offset by a $6.7 million gain on the liquidation of the Rural Telephone Bank (RTB), and a $2.0 million gain on the purchase of the Alaska terrestrial assets from Crest Communications, LLC. In 2007 we incurred $0.4 million in loss on the extinguishment of debt and recorded $0.6 million for gains from the RTB liquidation that are payable to our regulated intrastate wireline customers.

Income Taxes: In the year ended December 31, 2007, we generated taxable income which was offset by net operating loss carry forwards. We did, however, incur an alternative minimum tax charge of $0.5 million for the same period. Prior to December 31, 2007, we had fully reserved the unused income tax benefit resulting from the consolidated losses we have incurred since May 14, 1999, the date of the acquisition of substantially all of our operations. In 2007, the Company reversed all of its valuation allowance of $122.5 million as management now believes it is more likely than not, that all of the deferred tax asset will be realized based on the weight of all available evidence, including the last two years of earnings as well as projected earnings.

Net Income: The increase in net income is primarily a result of the one-time reversal of the valuation allowance against our deferred tax asset in 2007.

Liquidity and Capital Resources

Sources

We have satisfied our cash requirements for the year ended December 31, 2008 for operations, capital expenditures and debt service primarily through internally generated funds and the execution of a new convertible debt offering. For the year ended December 31, 2008, our net cash flows provided by operating activities were $94.6 million. At December 31, 2008, we had approximately $14.2 million in net working capital, approximately $1.3 million in cash and cash equivalents; and $20.5 million in restricted cash. As of December 31, 2008, we had $40.0 million of remaining capacity under our revolving credit facility, representing 89% of available capacity. During 2008 we invested excess cash in auction rate securities. Uncertainties in the credit markets have resulted in failed auctions for our entire existing portfolio of auction rate securities of $1.0 million, net of impairment loss. These investments are no longer considered liquid and during the year we took a $0.2 million other-than-temporary impairment charge to the income statement. For further information on our investment in auction rate securities, see

Item 7A Quantitative and Qualitative Disclosures about Market Risk Liquidity Risk and Item 1A Risk Factors .

As of December 31, 2008, total long-term obligations outstanding, including current portion, were $561.5 million consisting of a $425.9 million draw from our 2005 senior credit facility, a $5.0 million draw on our revolving credit facility of $45.0 million, $125.0 million of convertible notes and $5.6 million in finance lease obligations. The $425.9 million term loan under the 2005 senior credit facility was drawn on February 1, 2005, July 15, 2005, and February 22, 2006 and generally bears interest at an annual rate of London Inter-Bank Offered Rate (LIBOR) plus 1.75%, with a term of seven years from the first closing date and no scheduled principal payments before maturity. The $5.0 million draw on our revolving credit facility generally bears interest at LIBOR plus 2.00%. To the extent a portion of the revolving credit facility under the 2005 senior credit facility remains undrawn, we will pay an annual commitment fee of 0.375% of the undrawn principal amount over its term. We also entered into floating-to-fixed interest rate swaps with total notional amounts of approximately $135.0 million, $85.0 million, $40.0 million, $115.0 million and $52.9 million. This swaps the floating interest rate on the entire term loan borrowings under the 2005 senior credit facility for a further one to three years at a fixed rate of 5.88%, 6.25%, 6.18%, 6.71% and 6.75% per year, respectively, inclusive of the 1.75% premium over LIBOR. The swaps are accounted for as cash flow hedges.

Our 2005 senior secured credit facility contains a number of restrictive covenants and events of default, including covenants limiting capital expenditures, incurrence of debt and payment of dividends. The 2005 senior credit facility also requires that we achieve certain financial ratios quarterly and we are currently operating comfortably within these restrictions.

Uses

Our networks require the timely maintenance of plant and infrastructure. Our historical capital expenditures have been significant. The construction and geographic expansion of our wireless network and our AKORN submarine fiber have required significant capital. The implementation of our interexchange network and data services strategy is also capital intensive. New capital acquisition for 2008 totaled $125.7 million, inclusive of $3.4 million in interest capitalized during the course of construction. Exclusive of capitalized interest, $39.5 million was expended on recurring maintenance capex requirements; $82.4 million was expended on the construction of our long-haul fiber facilities which once complete will provide telecommunication connectivity between the lower 48 states and Alaska as well as provide geographically diverse connectivity between Anchorage and Fairbanks; and $0.4 million was expended on capex that is reimbursable from the selling stockholders of Crest. During 2008 we acquired Crest Communications in an all cash transaction deal that totaled $65.0 million, net of $1.1 million in cash acquired and inclusive of $4.2 million of cash consideration that has been placed in an escrow account for the settlement of any potential claims of misrepresentations, breach of warranties or covenants or for other indemnifications during the first eighteen months following the closing. We intend to fund $4.2 million due to the former stockholders of Crest and future capital expenditures, including the completion of our long-haul fiber build to the lower 48 states which we estimate will cost approximately $7.8 million to complete, exclusive of capitalized interest expense and internal overhead allocations with cash on hand, through internally generated cash flows, access to our restricted cash balance and borrowings under our revolving credit facility.

Our capital requirements may change due to impacts of regulatory decisions that affect our ability to recover our investments, changes in technology, the effects of competition, changes in our business strategy, and our decision to pursue specific acquisition and investment opportunities, among other things.

Cash interest expense, net of cash interest income, for 2008 totaled $29.5 million. Through a series of interest rate swap transactions, interest on our term loan is effectively fixed at an annual rate of 6.3% while our $125.0 million convertible debt has a fixed coupon of 5.75%.

From time to time we make purchases of our outstanding debt securities on the open market, in negotiated transactions or on available call dates. The timing and amount of such purchases, if any, depend upon cash needs and market conditions, among other things. Under the terms of our term loan we may also be required to make certain prepayments based on annual gains in our restricted payment baskets. In 2008 we paid down $2.0 million of our term loan.

On October 28, 2004, we announced the adoption of a dividend policy by our Board of Directors and declared our first quarterly dividend of $0.185 per share. On March 21, June 14, September 16, and November 29, 2005, our

Board of Directors declared quarterly cash dividends of $0.20 per share. In February 2006, we announced our Board of Directors increased our dividend policy to an annual rate of $0.86 per share, an increase of 7.5% over the previous annual rate of $0.80 per share. Based on current shares outstanding at February 20, 2008 of approximately 43.7 million shares, and our current dividend of $0.86 per share, our current annual dividend commitment is $37.6 million. Dividends on our common stock are not cumulative.

We believe that we will have sufficient cash provided by operations, and available borrowing capacity under our revolving credit facility to service our debt, pay our quarterly dividends and fund our operations, capital expenditures and other obligations over the next 12 months. Our ability to meet such obligations will be dependent upon our future financial performance, which is, in turn, subject to future economic conditions and to financial, business, regulatory, and other factors, many of which are beyond our control.

Contractual Obligations

Current accounting standards require us to disclose our material obligations and commitments to making future payments under contracts, such as debt and lease agreements, and under contingent commitments, such as debt guarantees. We disclose our contractual long-term debt repayment obligations in Note 10 Long-term Obligations and our capital and operating lease payments in Note 6 Property, Plant and Equipment , in our consolidated financial statements provided in this report.

Our contractual obligations as of December 31, 2008, are in the following table. Generally, long-term liabilities are included in the table based on the year of required payment or an estimate of the year of payment. Such estimates of payment are based on a review of past trends for these items, as well as a forecast of future activities. Certain items were excluded from the following table where the year of payment is unknown and could not be reliably estimated.

Many of our other non-current liabilities have been excluded from the following table due to the uncertainty of the timing of payments, combined with the absence of historical trending to be used as a predictor of such payments.

	Total	2009	2010-2011	2012-2013	Thereafter
Long-term debt	$ 555,889	$	$ 5,000	$ 550,889	$
Interest on long-term debt	114,839	35,346	67,953	10,935	605
Capital leases	5,634	666	1,557	1,547	1,864
Operating leases	89,876	7,617	12,709	10,422	59,128
Unconditional purchase obligations	53,204	18,325	17,766	12,594	4,519
Total contractual cash obligations	$ 819,442	$ 61,954	$ 104,985	$ 586,387	$ 66,116

Off-Balance Sheet Arrangements

We have no special purpose or limited purpose entities that provide off-balance sheet financing, liquidity, or market or credit risk support, and we do not engage in leasing, hedging, research and development services, or other relationships that expose us to any significant liabilities that are not reflected on the balance sheet or in Contractual Obligations above.

Critical Accounting Policies and Estimates

We have identified certain policies and estimates as critical to our business operations and the understanding of our past or present results of operations. For additional discussion on the application of these and other significant accounting policies, see Note 1 Summary of Significant Accounting Policies to our consolidated financial statements provided in this report. These policies and estimates are considered critical because they had a material impact, or they have the potential to have a material impact, on our financial statements and because they require significant judgments, assumptions or estimates.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Among the significant estimates affecting the financial statements are those related to the realizable value of accounts receivable, materials and supplies, long-lived assets, goodwill and intangible assets, income taxes and network access revenue reserves. Actual results may differ from those estimates.

Regulatory and Intercompany Accounting

Our consolidated financial statements include all majority-owned subsidiaries. We and our subsidiaries follow, where applicable, SFAS No. 71, *Accounting for the Effects of Certain Types of Regulation*. Our local telephone

company subsidiaries charge other subsidiaries based on regulated rates for telecommunications services. Intercompany revenue between regulated local telephone companies and all other subsidiaries is not eliminated upon consolidation. Other intercompany balances are eliminated upon consolidation.

36

Our local telephone company subsidiaries account for costs in accordance with the accounting principles prescribed by SFAS No. 71. This accounting recognizes the economic effects of rate regulation by recording cost and a return on investment as such amounts are recovered through rates authorized by regulatory authorities. Accordingly, plant and equipment is depreciated over lives approved by regulators and certain costs and obligations are deferred based upon approvals received from regulators to permit recovery of such amounts in future years.

We implemented, effective January 1, 2003, higher depreciation rates for our interstate telephone plant, which management believes approximate the economically useful lives of the underlying plant. As a result, we recorded a regulatory asset under SFAS No. 71, as of December 31, 2008 and 2007, related to depreciation of the regulated telephone plant allocable to its intrastate and local jurisdictions. If we were not following SFAS No. 71, these costs would have been charged to expense as incurred. The balances at December 31, 2008 and December 31, 2007, are $63.4 and $65.3 million, respectively. We also have a regulatory liability of $64.1 million and $62.4 million at December 31, 2008 and 2007, respectively, related to accumulated removal costs for our local telephone subsidiaries. If we were not following SFAS No. 71, we would have followed SFAS No. 143 for asset retirement obligations associated with our regulated telephone plant. Non-regulated revenues and costs incurred by the local telephone exchange operations and non-regulated operations are not accounted for under SFAS No. 71. In accordance with industry practice and regulatory requirements, revenues generated between regulated and non-regulated group companies are not eliminated on consolidation; these revenues totaled $41.6 million, $38.4 million, and $32.8 million, for the years ended December 31, 2008, 2007 and 2006, respectively.

The methodologies discussed above for determining regulated rates and the resulting revenue and charges are based on rules adopted by the RCA. We believe the accounting estimates related to affiliate revenue and charges are critical accounting estimates because determining the cost allocation methodology and the supporting allocation factors: (i) requires judgment and is subject to refinement as facts and circumstances change or as new cost drivers are identified; (ii) are based on regulatory rules which are subject to change; and (iii) the various subsidiaries may change provided services which can impact overall costs and related charges, all of which require significant judgment and assumptions and can affect consolidated results.

Should our local exchange businesses cease to be subject to rate regulation we would implement SFAS 101 "*Accounting for Discontinuation of Application of SFAS 71*.

We believe that application of SFAS 101 would result in a reduction in our regulatory assets and liabilities and the elimination of certain intercompany revenues and expenses. In addition, we would recognize extraordinary income (loss) in the fiscal quarter where SFAS 71 is no longer applied. The adjustment would be required to account for the change to recording expense on a non-regulated GAAP basis rather than a regulatory basis.

We have filed with the FCC a petition to be re-characterized from a rate of return carrier to a price cap carrier. If our petition is granted, SFAS 71 would no longer apply to our regulated entities. We believe our petition is likely to be granted, in which case we would be required to make the changes generally described above. We have not yet quantified the effect of this change; however, this change in regulatory accounting may cause our financial condition to appear to be adversely affected.

Revenue Recognition Policies

We recognize revenue for recurring services when earned, which is usually on a month-to-month basis. We also recognize non-recurring revenues, including activation fees and usage sensitive charges, when earned. Where we have determined that certain bundled products, including coupled wireline and wireless services, constitute arrangements with multiple deliverables, we allocate and measure using units of accounting and our judgment within the arrangement based on relative fair values.

Additionally, we establish a bad debt reserve against uncollectible revenues incurred during the period. These estimates are derived through a quarterly analysis of account aging profiles and a review of historical recovery experience. The reserve is adjusted when receivables are deemed to be uncollectible or otherwise paid. We account for bad debt expense in accordance with SFAS No. 71 which prescribes that revenue be recognized net of bad debt expense.

We recognize access revenue when it is earned. We participate in access revenue pools with other telephone companies. Such pools are funded by toll revenue and/or access charges regulated by the FCC within the interstate

jurisdiction. Much of the interstate access revenue is initially recorded based on estimates. These estimates are derived from interim financial statements, available separations studies and the most recent information available about achieved rates of

return. These estimates are subject to adjustment in future accounting periods as additional operational information becomes available for the Company and the other telephone companies. To the extent that disputes arise over revenue settlements, we defer revenue collected until settlement methodologies are resolved and finalized. At December 31, 2008 and 2007, the Company had recorded liabilities of $6.4 million and $11.0 million, respectively, related to its estimate of refundable access revenue. The decrease in the reserve during the year ended December 31, 2008 of $4.6 million was the result of refunds, the settlement of prior period claims and positive settlements with NECA and USAC regarding our cost studies.

Debt Issuance Costs and Original Issue Discounts

We amortize using the straight-line method underwriting and issuance costs associated with the issuance of our senior credit facility, convertible notes and senior unsecured notes over the term of the debt, which approximates the effective interest method. During 2008. the Company executed a new convertible debt offering that resulted in debt issuance costs of $4.4 million. During 2007 and 2006, the Company repurchased its 2011 senior unsecured notes resulting in a write off of debt issuance costs in 2007 and 2006 of $0.1 million and $1.7 million, respectively. Debt issuance cost amortization, inclusive of the write-offs, in the Consolidated Statement of Cash Flows for 2008, 2007 and 2006, was $2.5 million, $2.0 million and $3.6 million, respectively.

We have issued certain debt instruments below their face value, resulting in original issue discounts that we record net in long-term debt. These original issue discounts are amortized using the effective interest method. During 2007 and 2006, the Company repurchased its 2011 senior unsecured notes, which resulted in a write off of original issue discount to expense of $0.1 million and $1.5 million, respectively. Original issue discount, inclusive of the write offs, in the Consolidated Statement of Cash Flows for 2008, 2007 and 2006, was zero, $0.1 million and $1.5 million, respectively.

Income Taxes

We use the asset-liability method of accounting for income taxes. Under the asset-liability method, deferred taxes reflect the temporary differences between the financial and tax bases of assets and liabilities using the enacted tax rates in effect in the years in which the differences are expected to reverse. Deferred tax assets are reduced by a valuation allowance to the extent that management believes it is more likely than not that such deferred tax assets will not be realized. We released during the fourth quarter of 2007, in full, the existing valuation allowance against our deferred tax asset.

Non-Operating Expense

We periodically evaluate the fair value of our investments and other non-operating assets against their carrying value whenever market conditions indicate a change in that fair value. Any changes relating to declines in the fair value of non-operating assets are charged to non-operating expense under the caption Other in the Consolidated Statement of Operations . These items require significant judgment and assumptions. We believe our estimates are reasonable, based on information available at the time they were made. However, if our estimates are not correct or if circumstances underlying our estimates change, we may incur unexpected impairment charges in future periods.

Recently Adopted Accounting Pronouncements

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in accordance with GAAP and expands disclosures about fair value measurements. We adopted SFAS No. 157, effective January 1, 2008, for financial assets and financial liabilities, and other items recognized or disclosed in the consolidated financial statements on a recurring basis In February 2008, the FASB issued FSP SFAS 157-2, *Effective Date of FASB Statement No. 157*, which deferred the effective date of SFAS No. 157 for one year for certain nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis. In October 2008, the FASB also issued FSP SFAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active*, which clarifies the application of SFAS No. 157 in an inactive market and illustrates how an entity would determine fair value when the market for a financial asset is not active. On January 1, 2008, we adopted, without material impact on our consolidated financial statements, the provisions of SFAS No. 157 related to financial assets and liabilities and to nonfinancial assets and liabilities measured at fair value on a recurring basis. Beginning January 1, 2009, we will adopt the provisions required related to nonfinancial assets and nonfinancial liabilities that

are not required or permitted to be measured at fair value on a recurring basis, which include those measured at fair value in goodwill impairment testing, indefinite-lived intangible assets measured at fair value for impairment assessment, nonfinancial long-lived assets measured at fair value for impairment assessment, asset retirement obligations initially measured at fair value, and those initially measured at fair value in a business combination. We do not expect the provisions of SFAS No. 157 related to these items to have a material impact on our consolidated financial statements.

Recently Issued Accounting Pronouncements

In December 2007, the FASB issued SFAS No. 141(R), *Business Combinations*. SFAS No. 141(R) requires the recognition of all the assets acquired, liabilities assumed and any non-controlling interest in the acquiree at the acquisition date at fair value with limited exceptions. SFAS No. 141(R) requires that acquisition costs and restructuring costs associated with a business combination be expensed as incurred. This standard also requires that in-process research and development be recorded on the balance sheet at fair value as an indefinite-lived intangible asset at the acquisition date. In addition, under SFAS No. 141(R), changes in an acquired entity s valuation allowance on deferred tax assets and uncertain tax positions after the measurement period will impact income tax expense. SFAS No. 141(R) is effective on a prospective basis for all business combinations where the acquisition date occurs in or after the first fiscal year beginning on or after December 15, 2008, with the exception of the accounting for valuation allowances on deferred taxes and acquired uncertain tax positions. Upon the implementation of SFAS No. 141(R), any reduction in these valuation allowances will be recorded as a reduction to income tax expense.

In December 2008, the FASB issued FASB Staff Position No. FAS 132(R)-1, *Employers Disclosures about Postretirement Benefit Plan Assets* (FSP FAS 132(R)-1). FSP FAS 132(R)-1 amends FASB Statement No. 132 (revised 2003), *Employers Disclosures about Pensions and Other Postretirement Benefits*, (FAS 132(R)), to provide guidance on an employer s disclosures about plan assets of a defined benefit pension or other postretirement plan. The additional disclosure requirements under this FSP include expanded disclosures about an entity s investment policies and strategies, the categories of plan assets, and concentrations of credit risk and fair value measurements of plan assets. We anticipate that the adoption of this statement will not have a material impact on our consolidated financial statements, but will require additional footnote disclosures.

In June 2008, the FASB issued Staff Position (FSP) Emerging Issues Task Force (EITF) Issue No. 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities* (FSP No. EITF 03-6-1), in which the FASB concluded that all outstanding unvested share-based payment awards that contain rights to nonforfeitable dividends or dividend equivalents (such as restricted stock units granted by the Company) are considered participating securities. Because the awards are considered participating securities, the issuing entity is required to apply the two-class method of computing basic and diluted earnings per share. The provisions of FSP No. EITF 03-6-1 became effective for us on January 1, 2009 are applied retrospectively to all prior-period earnings per share computations. The adoption of FSP No. EITF 03-6-1 will not have a material impact on earnings per share amounts in prior periods.

In May 2008, the FASB issued FASB Staff Position APB 14-1 *Accounting for Convertible Debt Instruments That May Be Settled Upon Conversion (Including Partial Cash Settlement)* (FSP APB 14-1). This new standard requires the initial proceeds from convertible debt that may be settled in cash to be bifurcated between a liability component and an equity component. The objective of the guidance is to require the liability and equity components of convertible debt to be separately accounted for in a manner such that the interest expense recorded on the convertible debt would not equal the contractual rate of interest on the convertible debt, but instead would be recorded at a rate that would reflect the issuer s conventional non-convertible debt borrowing rate at the date of issuance. This is accomplished through the creation of a discount on the debt that would be accreted using the effective interest method as additional non-cash interest expense over the period the debt is expected to remain outstanding. The provisions of FSP APB 14-1 will be applied retrospectively to all periods presented for fiscal years beginning after December 31, 2008. We expect the adoption of FSP APB 14-1 to increase the interest expense on our 5.75% Convertible Notes due 2013 recorded in our results of operations by an annual amount of approximately $6.6 million.

In June 2008, the FASB ratified EITF Issue 07-5, *Determining Whether an Instrument (or Embedded Feature) Is Indexed to an Entity s Own Stock* (EITF 07-5). Paragraph 11(a) of Statement of Financial Accounting Standard No 133, Accounting for Derivatives and Hedging Activities (SFAS 133) specifies that a contract that would otherwise meet the definition of a derivative, but is both (a) indexed to the Company s own stock and (b) classified in stockholders equity in the statement of financial position would not be considered a derivative financial instrument. EITF 07-5 provides a new two-step model to be applied in determining whether a financial instrument or an embedded feature is indexed to an issuer s own stock and thus able to qualify for the SFAS 133 paragraph 11(a) scope exception. EITF 07-5 will be effective for the first annual reporting period beginning after December 15, 2008, and

early adoption is prohibited. We are currently evaluating whether the adoption of EITF 07-5 will have an impact on our accounting for our 5.75% Convertible Notes due 2013 and related derivative hedge transactions we entered into in connection with our offering of the notes.

In April 2008, the FASB issued FSP FAS 142-3, *Determination of the Useful Life of Intangible Assets*. FSP FAS 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, *Goodwill and Other Intangible Assets*. FSP FAS 142-3 is effective for fiscal years, or interim periods, beginning after December 15, 2008. The guidance contained in FSP FAS 142-3 for determining the useful life of a recognized intangible asset shall be applied prospectively to intangible assets acquired after the effective date. However, the disclosure requirements of FSP FAS 142-3 must be applied prospectively to all intangible assets recognized in our financial statements as of the effective date. The adoption of FSP FAS 142-3 is not expected to have a material impact on our consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities* an Amendment of FASB Statement 133. SFAS No. 161 enhances derivative and hedging activity disclosures pertaining to how derivative instruments are used, how derivative instruments and related hedged items are accounted for under SFAS No. 133, and how derivative instruments and related hedged items affect the Company s consolidated financial statements. SFAS No. 161 is effective for fiscal years, and interim periods, beginning after November 15, 2008. We do not anticipate that the adoption of SFAS No. 161 will have a material impact on our consolidated financial statements.

Table of Contents

Item 7A. Quantitative and qualitative disclosures about market risk

As of December 31, 2008, we had outstanding our 2005 senior credit facility, partial draw on our revolver, and convertible notes. These on-balance sheet financial instruments, to the extent they provide for variable rates of interest, expose us to interest rate risk, with the primary interest rate risk exposure resulting from changes in LIBOR or the prime rate, which are used to determine the interest rates that are applicable to borrowings under our 2005 senior credit facility and revolver.

The table below provides information about our sensitivity to market risk associated with fluctuations in interest rates as of December 31, 2008. To the extent that our financial instruments expose us to interest rate risk, they are presented within each market risk category in the table below. The table presents principal cash flows and related expected interest rates by year of maturity for our 2005 senior credit facility, 5.75% convertible notes due in 2013, and capital leases and other long-term obligations outstanding at December 31, 2008. Weighted average variable rates for the 2005 senior credit facility are based on implied forward rates in the LIBOR yield curve as of December 31, 2008. Fair values as of December 31, 2008 included herein have been determined based on (i) quoted market prices for the 2005 senior secured credit facility; and (ii) quoted market prices for the 5.75% convertible notes. Our consolidated financial statements contain descriptions of the 2005 senior credit facility, 5.75% convertible notes and capital leases and other long-term obligations and should be read in conjunction with the table below.

($ in thousands)	2009	2010	2011	2012	2013	Thereafter	Total	Fair Value
Interest Bearing Liabilities								
2005 bank credit facility	$	$	$	$425,889	$	$	$425,889	$340,711
Weighted average interest rate (var)	2.98%	3.42%	4.04%	4.26%			3.50%	
Revolver draw	$	$	$ 5,000	$	$	$	$ 5,000	$ 4,000
Weighted average interest rate (var)	3.23%	3.67%	4.12%				3.48%	
5.75% convertible notes due 2013	$	$	$	$125,000	$	$	$125,000	$ 93,013
Average interest rate (fixed)	5.75%	5.75%	5.75%	5.75%			5.75%	
Captial lease and other long-term	$ 666	$ 737	$ 820	$ 903	$ 644	$1,864	$ 5,634	$ 5,634
Average interest rate (fixed)	10.21%	10.28%	10.38%	10.57%	10.78%	10.87%	10.49%	
Interest Rate Derivatives								
Variable to fixed interest rate swap								

Notional amount	$67,500	$	$	$	$	$	$ 67,500	$ (1,863)
Fixed rate payable	4.13%						4.13%	
Weighted average variance Rate receivable (payable)	-2.90%						-2.90%	
Notional amount	$67,500	$	$	$	$	$	$ 67,500	$ (1,863)
Fixed rate payable	4.13%						4.13%	
Weighted average variance Rate receivable (payable)	-2.90%						-2.90%	
Notional amount	$	$85,000	$	$	$	$	$ 85,000	$ (3,222)
Fixed rate payable	4.50%	4.50%					4.50%	
Weighted average variance Rate receivable (payable)	-3.27%	-3.07%					-3.23%	
Notional amount	$	$	$ 40,000	$	$	$	$ 40,000	$ (2,685)
Fixed rate payable	4.43%	4.43%	4.43%				4.43%	
Weighted average variance Rate receivable (payable)	-3.19%	-2.76%	-2.26%				-2.78%	
Notional amount	$	$	$115,000	$	$	$	$115,000	$ (9,752)
Fixed rate payable	4.96%	4.96%	4.96%				4.96%	
Weighted average variance Rate receivable (payable)	-3.73%	-3.29%	-2.67%				-3.23%	
Notional amount	$	$	$ 52,900	$	$	$	$ 52,900	$ (4,532)
Fixed rate payable	5.00%	5.00%	5.00%				5.00%	
Weighted average variance Rate receivable (payable)	-3.76%	-3.33%	-2.70%				-3.26%	
Total derivative fair value								$ (23,917)

The table below provides information about our sensitivity to market risk associated with fluctuations in interest rates as of December 31, 2007. To the extent that our financial instruments expose us to interest rate risk, they are presented within each market risk category in the table below. The table presents principal cash flows and related expected interest rates by year of maturity for our 2005 senior credit facility, senior unsecured notes, and capital leases and other long-term obligations outstanding at December 31, 2007. Weighted average variable rates for the 2005 senior credit facility are based on implied forward rates in the LIBOR yield curve as of December 31, 2007. Fair values as of December 31, 2007 included herein have been determined based on (i) quoted market prices for the 2005 senior secured credit facility; and (ii) quoted market prices for the senior unsecured notes. Our consolidated financial statements contain descriptions of the 2005 senior credit facility, senior unsecured notes and capital leases and other long-term obligations and should be read in conjunction with the table below:

($ in thousands)	2008	2009	2010	2011	2012	Thereafter	Total	Fair Value
Interest Bearing Liabilities								
2005 bank credit facility	$	$	$	$	$427,900	$	$427,900	$410,784
Weighted average interest rate (var)	6.15%	5.75%	5.87%	6.24%	6.46%		6.01%	
Captial lease and other long-term	$ 780	$ 609	$ 672	$ 739	$ 800	$1,496	$ 5,096	$ 5,096
Average interest rate (fixed)	10.20%	10.27%	10.38%	10.56%	10.95%	11.50%	10.61%	
Interest Rate Derivatives								
Variable to fixed interest rate swap								
Notional amount	$	$67,500	$	$	$	$	$ 67,500	$ (482)
Fixed rate payable	4.13%	4.13%					4.13%	
Weighted average variance Rate receivable (payable)	0.27%	-0.13%					0.07%	
Notional amount	$	$67,500	$	$	$	$	$ 67,500	$ (485)
Fixed rate payable	4.13%	4.13%					4.13%	
Weighted average variance Rate receivable (payable)	0.27%	-0.13%					0.07%	
Notional amount	$	$	$85,000	$	$	$	$ 85,000	$ (1,352)

Fixed rate payable	4.50%	4.50%	4.50%				4.50%	
Weighted average variance Rate receivable (payable)	-0.10%	-0.50%	-0.52%				-0.32%	
Notional amount	$	$	$	$ 40,000	$	$	$ 40,000	$ (669)
Fixed rate payable	4.43%	4.43%	4.43%	4.43%			4.43%	
Weighted average variance Rate receivable (payable)	-0.02%	-0.42%	-0.30%	0.04%			-0.19%	
Notional amount	$	$	$	$115,000	$	$	$115,000	$ (4,195)
Fixed rate payable	4.96%	4.96%	4.96%	4.96%			4.96%	
Weighted average variance Rate receivable (payable)	-0.56%	-0.96%	-0.84%	-0.47%			-0.71%	
Notional amount	$	$	$	$ 52,900	$	$	$ 52,900	$ (1,996)
Fixed rate payable	5.00%	5.00%	5.00%	5.00%			5.00%	
Weighted average variance Rate receivable (payable)	-0.59%	-0.99%	-0.87%	-0.50%			-0.74%	
Total derivative fair value								$ (9,179)

Liquidity Risk

We currently hold a $1.0 million portfolio of auction rate securities. These investments are not currently liquid and in the event we need to access these funds, we will not be able to do so without a loss of principal, unless a future auction on these investments is successful. During 2008, we concluded that these investments were other-than-temporarily impaired and an impairment charge was taken to the income statement of $245. We may need to access these funds for operational purposes during the time that these investments are expected to remain illiquid.

Table of Contents

Item 8. Financial Statements and Supplementary Data

Consolidated financial statements of Alaska Communications Systems Group, Inc. and Subsidiaries are submitted as a separate section of this Form 10-K. See Index to Consolidated Financial Statements and Schedule, which appears on page F-1 hereof.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None

ITEM 9A. CONTROLS AND PROCEDURES

(A) Evaluation of Disclosure Controls and Procedures.

Under supervision and with the participation of management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operation of its disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, as of December 31, 2008; and whether any change has occurred in our internal control over financial reporting pursuant to Exchange Act Rules 13a-15(d) and 15d-15(d). Based on this evaluation, our principal executive officer and principal financial officer concluded as of the Evaluation Date that the Company s disclosure controls and procedures were effective as of December 31, 2008.

(B) Management s Report on Internal Control over Financial Reporting.

Our management is responsible for establishing and maintaining adequate internal control over our financial reporting. Our internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with U.S. generally accepted accounting principles. Internal control over financial reporting includes policies and procedures that: (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with U.S. generally accepted accounting principles, and that our receipts and expenditures are being made only in accordance with authorizations of our management and directors; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of our assets that could have a material effect on the financial statements.

All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective may not prevent or detect misstatements.

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2008. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control-Integrated Framework.

Our management s assessment included an evaluation of such elements as the design and operating effectiveness of key financial reporting controls, process documentation, accounting policies, and overall control environment. Based on this assessment, management has concluded that the Company s internal control over financial reporting as of December 31, 2008 was effective.

(C) Changes in internal control over financial reporting.

There was no change in our internal control over financial reporting that occurred in the fourth quarter of 2008 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. Other Information

Not applicable.

Table of Contents

PART III

Item 10. Directors and Executive Officers of the Registrant

The information required by this item is contained in our Proxy Statement for our 2009 Annual Meeting of Stockholders and is incorporated herein by reference.

Code of Ethics

We have adopted a code of ethics that applies to our principal executive officer, principal financial officer, principal accounting officer, or controller, and persons performing similar functions. We will provide to any person, free of charge, a copy of such code of ethics. The request must be submitted in writing to the Corporate Secretary, Alaska Communications Systems Group, Inc., 600 Telephone Avenue, Anchorage, Alaska 99503.

Item 11. Executive Compensation Summary Compensation Table

Information on compensation of our directors and executive officers is contained in our Proxy Statement for our 2009 Annual Meeting of Stockholders.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Information with respect to security ownership of certain beneficial owners and management is incorporated herein by reference to information included in the Proxy Statement for our 2009 Annual Meeting of Stockholders.

Securities Authorized for Issuance under Equity Compensation Plans

As of December 31, 2008, the number of securities remaining available for future issuance under equity compensation plans includes 1,385,010 shares under the Alaska Communications Systems Group, Inc. 1999 Stock Incentive Plan, 116,503 shares under the ACS Group, Inc. 1999 Non-Employee Director Stock Compensation Plan, and 751,912 shares under the Alaska Communications Systems Group, Inc. 1999 Employee Stock Purchase Plan. All shares reserved under the non-qualified stock option agreement between Liane Pelletier and Alaska Communications Systems Group, Inc. have been awarded through stock options. The units reserved as restricted stock unit equivalents (RSUEs) have been awarded according to the terms of the amended and restated employment agreement between Alaska Communications Systems Group, Inc. and Liane Pelletier. The RSUEs will settle in common stock on July 31, 2009, unless stockholder approval is not obtained, in which case they will settle in cash. See Note 15 Stock Incentive Plans , to the Alaska Communications Systems Group, Inc. Consolidated Financial Statements for further information on our equity compensation plans.

Equity compensation plans	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Approved by security holders:			
Stock options	1,150,549	$ 9.71	
Restricted stock	1,382,067	$	2,253,425
Not approved by security holders:			
Stock options	200,000	$ 4.50	
Subject to future approval by security holders:			
Restricted stock unit equivalents	100,000	$	

Table of Contents

Item 13. Certain Relationships and Related Transactions

Information with respect to such contractual relationships is incorporated herein by reference to the information in the Proxy Statement for our 2009 Annual Meeting of Stockholders.

Item 14. Principal Accountant Fees and Services

Information on our audit committee s pre-approval policy for audit services, and information on our principal accountant fees and services is contained in our Proxy Statement for our 2009 Annual Meeting of Stockholders.

Table of Contents

PART IV

Item 15. Exhibits and Financial Statement Schedules

(a) 1. *Financial Statements*

Our consolidated financial statements are submitted as a separate section of this Form 10-K. See Index to Consolidated Financial Statements and Schedule which appears on page F-1 hereof.

2. *Financial Statement Schedule*

Our financial statement schedules for the Company and its subsidiaries are submitted as a separate section of this Form 10-K. See Index to Consolidated Financial Statements and Schedule which appears on page F-1 hereof.

(b) *Exhibits.* The exhibits to this report are listed below. Other than exhibits that are filed herewith, all exhibits listed below are exhibits of the Registrant and are incorporated herein by reference as exhibits thereto.

Exhibit No.	Exhibit	Where Located
2.1	Stock Purchase Agreement by and among Alaska Communications Systems Group, Inc. and Crest Communications Corporations Group, Inc. (Crest) the Selling Stockholder; and Donald J. Schroeder and Brooke Coburn dated April 1, 2008 Confidential treatment has been granted for certain portions marked *** of this Exhibit.	Exhibit 2.1 to Form 8-K (filed 8/07/2008)
3.1	Amended and Restated Certificate of Incorporation of the Registrant.	Exhibit to Form S-1/A file No. 333-888753 (filed 11/17/1999)
3.2	Amended and Restated By-Laws of the Registrant.	Exhibit 3.2 to Form 8-K (filed 9/18/2008)
4.1	Specimen of Common Stock Certificate.	Exhibit to Form S-1/A file No. 333-888753 (filed 11/17/1999)
4.2	Indenture, dated as of August 26, 2003, among Alaska Communications Systems Holdings, Inc., as Issuer, the Guarantors (as defined therein) and The Bank of New York, as trustee.	Exhibit 4.1 to Form S-4 file No. 333-109927 (filed 10/23/2003)
4.3	Supplemental Indenture to Indenture listed as Exhibit No. 4.11, dated January 25, 2005, among the Company, Alaska Communications Systems Holdings, Inc., the guarantor s party thereto and The Bank of New York, as trustee.	Exhibit 10.1 to Form 8-K (filed 1/26/2005)
4.4	Supplemental Indenture to Indenture listed as Exhibit No. 4.5, dated January 25, 2005,	Exhibit 10.2 to Form 8-K (filed 1/26/2005)

	among the Company, Alaska Communications Systems Holdings, Inc., the guarantors party thereto and The Bank of New York, as trustee.	
4.5	Supplemental indenture to Indenture listed as Exhibit No. 4.11, dated July 15, 2005, among the Registrant, Alaska Communications Systems Holdings, Inc., the guarantors party thereto and the Bank of New York, as trustee.	Exhibit 1.1 to Form 8-K (filed 7/21/2005)
4.6	Supplemental Indenture to Indenture listed as Exhibit No. 4.11, dated February 22, 2006, among the Company, Alaska Communications Systems Holdings, Inc., the guarantors party thereto and The Bank of New York, as trustee.	Exhibit 10.1 to Form 8-K (filed 2/27/2006)
4.7	Indenture dated April 8, 2008 by and among Alaska Communications Systems Group, Inc., the guarantors named therein, and The Bank of New York Trust Company, N.A., as trustee , with respect to 5.75% Convertible Notes due 2013.	Exhibit 4.1 to Form 8-K (filed 4/14/2008)
4.8	Registration Rights Agreement dated April 8, 2008 by and among Alaska Communications Systems Group, Inc., the guarantors named therein, and the Initial Purchasers (as defined therein).	Exhibit 4.2 to Form 8-K (filed 4/14/2008)
10.1*	ALEC Holdings, Inc. 1999 Stock Incentive Plan.	Exhibit 10.10 to Form S-4 file No. 333-82361 (filed 7/7/1999)

Exhibit No.	Exhibit	Where Located
10.2*	Alaska Communications Systems Group, Inc. 1999 Stock Incentive Plan.	Exhibit to Form S-1/A file No. 333-888753 (filed 11/17/1999)
10.3*	Alaska Communications Systems Group, Inc. 1999 Non-Employee Director Compensation Plan.	Exhibit to Form S-1/A file No. 333-888753 (filed 11/17/1999)
10.4*	Alaska Communications Systems Group, Inc. 1999 Employee Stock Purchase Plan.	Exhibit to Form S-1/A file No. 333-888753 (filed 11/17/1999)
10.5*	Amended and Restated Employment Agreement, dated as of September 22, 2008, between Alaska Communications Systems Group, Inc. and Liane Pelletier.	Exhibit 10.1 to Form 8-K (filed 9/26/2008)
10.6	Settlement Agreement and Mutual Release, dated October 14, 2003, by and between the State of Alaska and Alaska Communications Systems Group, Inc.	Exhibit 10.4 to Form S-4 file No. 333-109927 (filed 10/23/2003)
10.7*	Executive Employment Agreement, dated as of January 23, 2004 between Alaska Communications Systems Group, Inc. and Sheldon Fisher.	Exhibit 10.13 to Form 10-K (filed 3/30/2004)
10.8*	Amended and Restated Employment Agreement, dated as of January 5, 2009 between Alaska Communications Systems Group, Inc. and David Wilson.	Exhibit 10.1 to Form 8-K (filed 01/09/2009)
10.9	Letter Agreement, dated January 26, 2005, between Alaska Communications Systems Holdings, Inc. and Fox Paine & Company, LLC.	Exhibit 10.1 to Form 8-K (filed 1/27/2005)
10.10	Credit Agreement, dated February 1, 2005, among the Company, ACSH, the lenders named therein and Canadian Imperial Bank of Commerce, as Administrative Agent.	Exhibit 10.1 to Form 8-K (filed 2/2/2005)
10.11	Master Agreement, dated November 7, 1999, by and between Alaska Communications Systems Holdings, Inc. and the International Brotherhood of Electrical Workers, Local Union 1547.	Exhibit 99.3 to Form 8-K (filed 3/7/2005)

10.12	Letter Agreement, dated March 1, 2005, by and between Alaska Communications Systems Holdings, Inc. and the International Brotherhood of Electrical Workers, Local Union 1547.	Exhibit 99.4 to Form 8-K (filed 3/7/2005)
10.13	Consent and Agreement No. 1, dated July 15, 2005, among Alaska Communications Systems Group, Inc. , Alaska Communications Systems Holdings, Inc., the lenders party thereto and Canadian Imperial Bank of Commerce as Administrative Agent.	Exhibit 1.1 to Form 8-K (filed 7/21/2005)
10.14*	Form of Restricted Stock Agreement between the Registrant and certain participants in the Registrant s 1999 Stock Incentive Plan.	Exhibit 10.1 to Form 10-Q (filed 8/3/2007)
10.15	Consent and Agreement No. 2, dated February 22, 2006, among Alaska Communications Systems Group, Inc. , Alaska Communications Systems Holdings, Inc., the lenders party thereto and Canadian Imperial Bank of Commerce as Administrative Agent.	Exhibit 10.2 to Form 8-K (filed 2/27/2006)
10.16*	2006 Officer Severance Program.	Exhibit 99.1 to Form 8-K (filed 7/17/2006)
10.17*	2008 Officer Severance Policy.	Exhibit 10.2 to Form 8-K (filed 12/24/2008)
10.18	Supply and Construction Contract between ACS Cable Systems, Inc. and Tyco Telecommunications (US), Inc. dated October 23, 2007***.	Exhibit 10.23 to Form 10-K (filed 3/20/2008)
10.19*	Executive Employment Agreement, dated as of November 7, 2007 between Alaska Communications Systems Group, Inc. and Leonard Steinberg.	Exhibit 10.24 to Form 10-K (filed 3/20/2008)
10.20	Purchase Agreement dated April 2, 2008 by and among Alaska Communications Systems Group, Inc., the guarantors listed therein and the Initial Purchasers.	Exhibit 10.1 to Form 8-K (filed 4/14/2008)

Table of Contents

Exhibit No.	Exhibit	Where Located
10.21	Confirmations of Convertible Bond Hedges by and between Alaska Communications Systems Group, Inc. and certain affiliates of the Initial Purchasers.	Exhibit 10.2 to Form 8-K (filed 4/14/2008)
10.22	Confirmations of Warrant Transactions by and between Alaska Communications Systems Group, Inc. and certain affiliates of the Initial Purchasers.	Exhibit 10.3 to Form 8-K (filed 4/14/2008)
10.23*	Form of Performance Share Unit Agreement.	Exhibit 99.1 to Form 8-K/A (filed 6/12/2008)
10.24*	Executive Employment Agreement, dated as of December 19, 2008 between Alaska Communications Systems Group, Inc. and Anand Vadapalli.	Exhibit 10.1 to Form 8-K (filed 12/24/2008)
21.1	Subsidiaries of the Registrant.	Filed herewith
23.1	Consent of KPMG LLP relating to the audited financial statements of Alaska Communications Systems Group, Inc.	Filed herewith
31.1	Certification of Liane Pelletier, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Filed herewith
31.2	Certification of David Wilson, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Filed herewith
32.1	Certification of Liane Pelletier, Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted to Section 906 of the Sarbanes-Oxley Act of 2002.	Filed herewith
32.2	Certification of David Wilson, Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted to Section 906 of The Sarbanes-Oxley Act of 2002.	Filed herewith

* Management contract or compensatory

plan or arrangement required to be filed as an exhibit to this form.

*** Confidential treatment of certain portions of this exhibit has been requested pursuant to a request for confidential treatment filed with the Securities and Exchange Commission. Omitted portions have been filed separately with the Commission.

Table of Contents

SIGNATURES

Pursuant to the requirements of Section 13 or Section 15(d) of the Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.
Date: March 9, 2009

Alaska Communications Systems Group, Inc.

By: /s/ Liane Pelletier
Liane Pelletier
Chief Executive Officer,
Chairman of the Board and President

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
/s/ Liane Pelletier Liane Pelletier	Chief Executive Officer, Chairman of the Board and President (Principal Executive Officer)	March 9, 2009
/s/ David Wilson David Wilson	Senior Vice President and Chief Financial Officer (Principal Financial and Accounting Officer)	March 9, 2009
/s/ Annette M. Jacobs Annette M. Jacobs	Director	March 9, 2009
/s/ Brian Rogers Brian Rogers	Director	March 9, 2009
/s/ David A. Southwell David A. Southwell	Director	March 9, 2009
/s/ John M. Egan John M. Egan	Director	March 9, 2009
/s/ Peter Ley Peter Ley	Director	March 9, 2009
/s/ Gary R. Donahee Gary R. Donahee	Director	March 9, 2009
/s/ Edward J. Hayes, Jr. Edward J. Hayes, Jr.	Director	March 9, 2009

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND SCHEDULE

Reports of Independent Registered Public Accounting Firm	F-2
Consolidated Balance Sheets December 31, 2008 and 2007	F-4
Consolidated Statements of Operations Years Ended December 31, 2008, 2007 and 2006	F-5
Consolidated Statements of Stockholders Equity (Deficit) and Comprehensive Income (Loss) Years Ended December 31, 2008, 2007 and 2006	F-6
Consolidated Statements of Cash Flows Years Ended December 31, 2008, 2007 and 2006	F-7
Notes to Consolidated Financial Statements Years Ended December 31, 2008, 2007 and 2006	F-8
Schedule II Valuation and Qualifying Accounts	F-41

Table of Contents

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Alaska Communications Systems Group, Inc.:

We have audited the accompanying consolidated balance sheets of Alaska Communications Systems Group, Inc. and subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of operation, stockholders equity (deficit) and comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2008. These consolidated financial statements are the responsibility of the Company s management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Alaska Communications Systems Group, Inc. and subsidiaries as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Alaska Communications System s Group, Inc. s internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated March 9, 2009 expressed an unqualified opinion on the effectiveness of the Company s internal control over financial reporting.

(signed) KPMG LLP
Anchorage, Alaska
March 9, 2009

Table of Contents

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Alaska Communications Systems Group, Inc.:

We have audited Alaska Communications Systems Group, Inc. s internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. Alaska Communications Systems Group, Inc. s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management s Report on Internal Control Over Financial Reporting (Item 9A.(B)). Our responsibility is to express an opinion on the Company s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Alaska Communications Systems Group, Inc. maintained, in all material respects, effective internal control over financial reporting as of December 31, 2008, based on criteria established in *Internal Control Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Alaska Communications Systems Group, Inc. and subsidiaries as of December 31, 2008 and 2007, and the related consolidated statements of operations, stockholders equity (deficit) and comprehensive income (loss), and cash flows for each of the years in the three-year period ended December 31, 2008, and our report dated March 9, 2009 expressed an unqualified opinion on those consolidated financial statements.

(signed) KPMG LLP
Anchorage, Alaska
March 9, 2009

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Consolidated Balance Sheets
December 31, 2008 and 2007
(In Thousands, Except Per Share Amounts)

	2008	2007
Assets		
Current assets:		
Cash and cash equivalents	$ 1,326	$ 35,208
Restricted cash	20,517	2,589
Short-term investments		790
Accounts receivable-trade, net of allowance of $5,912 and $8,768	40,433	39,150
Materials and supplies	9,404	10,467
Prepayments and other current assets	6,515	5,155
Deferred income taxes	21,145	21,347
Total current assets	99,340	114,706
Property, plant and equipment	1,391,351	1,209,257
Less: accumulated depreciation and amortization	(891,899)	(825,663)
Property, plant and equipment, net	499,452	383,594
Non-current investments	1,005	
Goodwill	8,850	38,403
Intangible assets, net	24,118	21,604
Debt issuance cost	9,290	7,461
Deferred income taxes	114,831	96,095
Deferred charges and other assets	452	1,340
Total assets	$ 757,338	$ 663,203
Liabilities and Stockholders Equity (Deficit)		
Current liabilities:		
Current portion of long-term obligations	$ 666	$ 780
Accounts payable, accrued and other current liabilities	74,028	64,070
Advance billings and customer deposits	10,399	10,051
Total current liabilities	85,093	74,901
Non-current obligations, net of current portion	560,857	432,216
Other deferred credits and long-term liabilities	98,693	82,075
Total liabilities	744,643	589,192
Commitments and contingencies		
Stockholders equity (deficit):		
	437	429

Common stock, $.01 par value; 145,000 authorized, 43,719 and 42,883 issued and outstanding, respectively		
Additional paid in capital	217,740	257,982
Accumulated deficit	(187,452)	(177,313)
Accumulated other comprehensive loss	(18,030)	(7,087)
Total stockholders equity (deficit)	12,695	74,011
Total liabilities and stockholders equity (deficit)	$ 757,338	$ 663,203

See Notes to Consolidated Financial Statements

F-4

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Consolidated Statements of Operations
Years ended December 31, 2008, 2007, and 2006
(In Thousands, Except Per Share Amounts)

	2008	2007	2006
Operating revenues:			
Wireline	$ 246,028	$ 248,265	$ 233,351
Wireless	143,569	137,520	115,370
Total operating revenues	389,597	385,785	348,721
Operating expenses:			
Wireline (exclusive of depreciation and amortization)	185,321	179,456	172,421
Wireless (exclusive of depreciation and amortization)	84,751	74,305	62,478
Depreciation and amortization	74,002	71,337	69,096
Loss on disposal of assets, net	750	248	1,105
Loss on impairment of goodwill and intangible assets	29,641		
Total operating expenses	374,465	325,346	305,100
Operating income	15,132	60,439	43,621
Other income and expense:			
Interest expense	(32,921)	(28,386)	(30,445)
Loss on extinguishment of debt		(355)	(9,650)
Interest income	1,695	2,020	1,835
Other	(547)	(776)	8,360
Total other income and expense	(31,773)	(27,497)	(29,900)
Income (loss) before income tax	(16,641)	32,942	13,721
Income tax benefit (expense)	6,502	111,194	(443)
Net income (loss)	$ (10,139)	$ 144,136	$ 13,278
Net income (loss) per share:			
Basic	$ (0.23)	$ 3.38	$ 0.32
Diluted	$ (0.23)	$ 3.26	$ 0.31
Weighted average shares outstanding:			
Basic	43,391	42,701	42,045

Diluted	43,391	44,185	43,387

See Notes to Consolidated Financial Statements

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Consolidated Statements of Stockholders Equity (Deficit)
and Comprehensive Income (Loss)
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

	Shares	Common Stock	Treasury Stock	Additional Paid in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (Loss)	Stockholders Equity (Deficit)
Balance, January 1, 2006	46,230	$ 462	$ (18,443)	$ 333,522	$ (334,727)	$ 322	$ (18,864)
Total comprehensive income					13,278	1,244	14,522
Dividends declared				(36,274)			(36,274)
Stock compensation				7,667			7,667
Surrender of 74 shares to cover withholding taxes on stock based compensation				(872)			(872)
Issuance of common stock, pursuant to stock plans, $.01 par	641	6		2,780			2,786
Retirement of stock held in treasury	(4,549)	(45)	18,443	(18,398)			
Balance, December 31, 2006	42,322	423		288,425	(321,449)	1,566	(31,035)
Total comprehensive income (loss)					144,136	(8,653)	135,483
Dividends declared				(36,840)			(36,840)
Stock compensation				6,390			6,390
Excess tax benefit from share-based payments				755			755
Surrender of 153 shares to cover withholding taxes on stock based compensation				(2,330)			(2,330)
Issuance of common stock,	561	6		1,582			1,588

pursuant to stock plans, $.01 par							
Balance, December 31, 2007	42,883	429		257,982	(177,313)	(7,087)	74,011
Total comprehensive income (loss)					(10,139)	(10,943)	(21,082)
Dividends declared				(37,523)			(37,523)
Stock compensation				8,770			8,770
Purchase of covertible bond call options net of tax benefits of $1,056				(19,375)			(19,375)
Sale of common stock warrants				9,852			9,852
Surrender of 273 shares to cover withholding taxes on stock-based compensation				(3,383)			(3,383)
Issuance of common stock stock, pursuant to stock plans, $.01 par	836	8		1,417			1,425
Balance, December 31, 2008	43,719	$ 437	$	$ 217,740	$ (187,452)	$ (18,030)	$ 12,695

See Notes to Consolidated Financial Statements

F-6

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Consolidated Statements of Cash Flows
Years Ended December 31, 2008, 2007 and 2006
(In Thousands)

	2008	**2007**	**2006**
Cash Flows from Operating Activities:			
Net income (loss)	$ (10,139)	$ 144,136	$ 13,278
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities:			
Depreciation and amortization	74,002	71,337	69,096
Loss on disposal of assets, net	750	248	1,105
Loss on impairment of goodwill and intangible assets	29,641		
Gain on sale of long-term investments		(152)	(6,685)
Loss on impairment of non-current investments	245		
Amortization of debt issuance costs and original issue discount	2,539	2,059	5,180
Stock-based compensation	9,477	6,390	7,667
Deferred income taxes	(6,445)	(112,495)	
Excess tax benefit from share-based payments		(755)	
Other non-cash expenses	139	742	234
Changes in components of assets and liabilities:			
Accounts receivable and other current assets	955	(1,896)	2,136
Materials and supplies	1,063	(2,490)	(92)
Accounts payable and other current liabilities	(2,102)	(1,607)	8,823
Deferred charges and other assets	470	(193)	3,856
Other deferred credits	(6,018)	(532)	(13,013)
Net cash provided by operating activities	94,577	104,792	91,585
Cash Flows from Investing Activities:			
Investment in construction and capital expenditures	(125,711)	(62,645)	(59,720)
Change in unsettled construction and capital expenditures	6,056	(509)	(915)
Investment in intangible assets	(2,601)		
Acquisitions, net of cash acquired	(64,960)		
Change in unsettled acquisition costs	4,169		
Purchase of short-term investments	(9,400)	(64,638)	(57,500)
Proceeds from sale of short-term investments	10,190	63,848	68,025
Purchase of non-current investments	(3,625)		
Proceeds from sale of non-current investments	2,375	162	7,663
Placement of funds in restricted accounts	(74,956)	(3,009)	
Release of funds from restricted accounts	57,028	2,120	2,715
Net cash used by investing activities	(201,435)	(64,671)	(39,732)
Cash Flows from Financing Activities:			
Repayments of long-term debt	(7,832)	(5,089)	(61,860)
Proceeds from the issuance of long-term debt	135,000		52,900
Purchase of call options	(20,431)		
Sale of common stock warrants	9,852		

Debt issuance costs	(4,368)		(1,349)
Payment of cash dividend on common stock	(37,287)	(36,697)	(35,475)
Payment of withholding taxes on stock-based compensation	(3,383)	(2,330)	(872)
Excess tax benefit from share-based payments		755	
Proceeds from the issuance of common stock	1,425	1,588	2,786
Net cash provided (used) by financing activities	72,976	(41,773)	(43,870)
Change in cash and cash equivalents	(33,882)	(1,652)	7,983
Cash and cash equivalents, beginning of period	35,208	36,860	28,877
Cash and cash equivalents, end of period	$ 1,326	$ 35,208	$ 36,860
Supplemental Cash Flow Data:			
Interest paid	$ 31,175	$ 28,795	$ 31,280
Income taxes paid	355	545	264
Supplemental Noncash Transactions:			
Property acquired under capital leases	$ 1,359	$ 51	60
Dividend declared, but not paid	9,449	9,226	9,105

See Notes to Consolidated Financial Statements

F-7

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

1. DESCRIPTION OF COMPANY AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Alaska Communications Systems Group, Inc. and Subsidiaries (the Company or ACS Group), a Delaware corporation, provides wireline, wireless and other telecommunications and network services to consumer, business, and enterprise customers in the State of Alaska and beyond using its statewide and interstate telecommunications network. The Company was formed in October of 1998 for the purpose of acquiring and operating telecommunications properties.

The accompanying consolidated financial statements for the Company are as of December 31, 2008 and 2007 and for the years ended December 31, 2008, 2007 and 2006. They represent the consolidated financial position, results of operations and cash flows of ACS Group and the following wholly owned subsidiaries:

Alaska Communications Systems Holdings, Inc. (ACS Holdings)

ACS of Alaska, Inc. (ACSAK)

ACS of the Northland, Inc. (ACSN)

ACS of Fairbanks, Inc. (ACSF)

ACS of Anchorage, Inc. (ACSA)

ACS Wireless, Inc. (ACSW)

ACS Long Distance, Inc. (ACSLD)

ACS Internet, Inc. (ACSI)

ACS Messaging, Inc. (ACSM)

ACS Cable Systems, Inc. (ACSC)

A summary of significant accounting policies followed by the Company is set forth below:

Basis of Presentation

The consolidated financial statements include all majority-owned subsidiaries. In accordance with Statement of Financial Accounting Standards (SFAS) No. 71, *Accounting for the Effects of Certain Types of Regulation*, intercompany revenue between regulated local telephone companies and all other group companies is not eliminated. All other significant intercompany balances have been eliminated. Certain reclassifications have been made to the 2007 and 2006 balances to conform to the current presentation.

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Among the significant estimates affecting the financial statements are those related to the realizable value of accounts receivable, long-lived assets, goodwill and intangible assets, legal contingencies, income taxes and network access revenue reserves. These estimates and assumptions are based on management s best estimates and judgment. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes is reasonable under the circumstances. Assumptions are adjusted as facts and circumstances dictate. Illiquid

credit markets, volatile equity and energy markets, and declines in consumer spending have combined to increase the uncertainty in such estimates and assumptions. As future events and their effects cannot be determined with precision, actual results may differ significantly from those estimates. Changes in those estimates resulting from continuing changes in the economic environment will be reflected in the financial statements of future periods.

Cash and Cash Equivalents

For purposes of the consolidated balance sheets and statements of cash flows, the Company generally considers all highly liquid investments with a maturity at acquisition of three months or less to be cash equivalents.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Restricted Cash

As of December 31, 2008, the Company had placed into escrow $9,739 for the indemnification of the Company in the event of breach by Crest Communications Corporation (Crest) of certain obligations, representations and warranties specified in the Company s agreement to purchase Crest and the completion of certain capital projects; and $8,578 pending completion by Tyco Telecommunications (Tyco) of specified milestones set forth in the Company s agreement with Tyco for the construction of its Alaska Oregon Network (AKORN) fiber optic cable system.

The remaining balance, as well as the prior year balance, consists of certificates of deposit as required under the terms of certain contracts to which the Company is a party. When the restrictions are lifted, the Company will transfer these funds back into its operating accounts.

Short-Term Investments

For purposes of the Consolidated Balance Sheets and Consolidated Statement of Cash Flows , the Company considers highly liquid investments with a maturity at acquisition of more than three months but less than one year to be short-term investments. These investments are classified as available for sale and are stated at estimated fair market value. Income related to these investments is reported as interest income.

Materials and Supplies

Materials and supplies are carried in inventory at the lower of weighted average cost or market. Cash flows related to the sale of inventory, primarily wireless devices and accessories, are included in operating activities in the Company s Consolidated Statement of Cash Flows .

Property, Plant and Equipment

Telephone plant is stated substantially at original cost of construction. Telephone plant retired in the ordinary course of business, together with the cost of removal, less salvage, is charged to accumulated depreciation with no gain or loss recognized. Renewals and betterments of telephone plant are capitalized while repairs, as well as renewals of minor items, are charged to operating expense as incurred. The Company provides for depreciation of telephone plant on the straight-line method, using rates approved by regulatory authorities. The composite annualized rate of depreciation for all classes of telephone property, plant, and equipment was 4.8%, 5.2% and 5.3% for 2008, 2007 and 2006, respectively.

Non-Telephone plant is stated at purchased cost, and when sold or retired a gain or loss is recognized. Depreciation of such property is provided on the straight-line method over its estimated service life ranging from three to 39 years.

The Company is the lessee of equipment and buildings under capital leases expiring in various years through 2019. The assets and liabilities under capital leases are initially recorded at the lower of the present value of the minimum lease payments or the fair value of the assets at the inception of the lease. The assets are amortized over the lower of their related lease terms or the estimated productive lives. Amortization of assets under capital leases is included in depreciation and amortization expense.

The Company is also the lessee of various land, building and personal property under operating lease agreements for which expense is recognized on a monthly basis. Increases in rental rates are recorded as incurred which approximates a straight-line method.

Non-current Investments

The Company s non-current investment balance is made up of auction rate securities (ARS). Beginning February 13, 2008, the Company experienced failed auctions for ARS issues and at that time, ceased to purchase auction rate securities. The Company believes that the current lack of liquidity relating to ARS investments will have no impact on the ability to fund ongoing operations and growth initiatives.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

At December 31, 2008, the Company s ARS portfolio was comprised of 100% AAA rated investments. Although the Company has the ability to hold these investments to maturity, an assessment was performed and management determined that the fair value of these securities was other-than-temporarily impaired. The Company has recorded a loss in the Consolidated Statements of Operations for the year ended December 31, 2008 of $245 related to its ARS portfolio. The Company will reassess this conclusion and the remaining portfolio balance in future reporting periods based on several factors, including the success or failure of future auctions, possible failure of the investment to be redeemed, deterioration of the credit ratings of the investments, market risk and other factors.

Goodwill and Intangible Assets

Goodwill and indefinite-lived intangible assets are not amortized but are assessed for impairment on at least an annual basis. In 2008, the Company took a charge for impairment to the goodwill balance on its wireline segment of $29,553 and intangibles of $88. See Note 8 Goodwill and Other Intangible Assets for information regarding the impairment charge recorded.

Debt Issuance Costs

Underwriting and issuance costs associated with the issuance of the Company s senior credit facility and senior unsecured notes are being amortized using the straight-line method, which approximates the effective interest method, over the term of the debt. During 2008, the Company executed a new convertible debt offering that resulted in debt issuance costs of $4,368. During 2007 and 2006, the Company repurchased its 2011 senior unsecured notes which resulted in a write-off of debt issuance costs in 2007 and 2006, of $84 and $1,731, respectively. Debt issuance cost amortization, inclusive of the write-offs, in the Consolidated Statement of Cash Flows for 2008, 2007 and 2006, was $2,539, $1,976 and $3,645, respectively.

Original Issue Discounts

Certain debt instruments of the Company have been issued below their face value, resulting in original issue discounts that are recorded net in long-term debt. These original issue discounts are amortized using the effective interest method. During 2007 and 2006, the Company repurchased its 2011 senior unsecured notes, which resulted in a write-off of original issue discount to expense of $72 and $1,479, respectively. Original issue discount, inclusive of the write-offs, in the Consolidated Statement of Cash Flows for 2008, 2007 and 2006, was zero, $83 and $1,535, respectively.

Capitalized Interest

The Company capitalizes interest charges to its construction in progress based on a weighted average interest cost calculated on the Company s outstanding debt. Interest expense for the year ended December 31, 2008, 2007 and 2006 was $32,921, $28,386 and $30,445, net of capitalized interest of $3,384, $1,904 and $807, respectively.

Preferred Stock

The Company has 5,000, no par, shares authorized, none of which were issued or outstanding at December 31, 2008 and 2007.

Treasury Stock

The Company, with Board of Directors authorization, occasionally repurchases shares of its common stock. Since management originally intended to hold the treasury stock temporarily for later re-issuance, the cost method of accounting for treasury stock was used. On December 15, 2006, the Company s Board of Directors approved the retirement of 100% of the Company s treasury stock.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition

Substantially all recurring service revenues are billed one month in advance and are deferred until earned. Non-recurring and usage sensitive revenues are billed in arrears and are recognized when earned. Certain of the Company s bundled products and services, primarily in wireless, have been determined to be revenue arrangements with multiple deliverables. Total consideration received in these arrangements is allocated and measured using units of accounting within the arrangement based on relative fair values. Wireless offerings include wireless phones and service contracts sold together in its Company owned stores. The handset and accessories associated with these direct channel sales is recognized at the time the related wireless phone is sold and is classified as equipment sales. Monthly service revenue is recognized as services are rendered.

The Company establishes estimated bad debt reserves against uncollectible revenues incurred during the period. These estimates are derived through a monthly analysis of account aging profiles and a review of historical recovery experience. Receivables are charged off against the allowance when management believes the uncollectability of the receivable is confirmed. Subsequent recoveries, if any, are credited to the allowance. The Company accounts for bad debt expense in accordance with SFAS No. 71 for regulated entities which prescribes that revenue be recognized net of bad debt expense.

Access revenue is recognized when earned. The Company participates in access revenue pools with other telephone companies. Such pools are funded by toll revenue and/or access charges regulated by the Federal Communications Commission (FCC) within the interstate jurisdiction. Much of the interstate access revenue is initially recorded based on estimates. These estimates are derived from interim financial statements, available separations studies and the most recent information available about achieved rates of return. These estimates are subject to adjustment in future accounting periods as additional operational information becomes available for the Company and the other telephone companies. To the extent that disputes arise over revenue settlements, the Company s policy is to defer revenue collected until settlement methodologies are resolved and finalized. At December 31, 2008 and 2007, the Company had deferred revenue of $6,372 and $10,992, respectively, related to its estimate of refundable access revenue. The decrease during the year ended December 31, 2008 of $4,620 was the result of refunds, the settlement of prior period claims and positive settlements with National Exchange Carrier s Association (NECA) and Universal Service Administration Corporation (USAC) regarding our cost studies.

Concentrations of Risk

Cash is maintained with several financial institutions. Deposits held with banks may exceed the amount of insurance provided on such deposits. Generally, these deposits may be redeemed upon demand. The Company has not experienced any losses on such deposits.

The Company performs credit evaluations of its suppliers and customers. The Company s customers do not, individually, represent a material concentration of risk. During 2008, 2007 and 2006, no customer accounted for 10% of consolidated revenues.

The Company also depends on a limited number of suppliers and vendors for equipment and services for its network, and in the case of the Company s wireless segment, billing processes. If these suppliers experience financial or credit difficulties, service interruptions, patent litigation, or other problems, subscriber growth the Company s operating results could be adversely affected.

Approximately 76% of the Company s employees are represented by the International Brotherhood of Electrical Workers, Local 1547 (IBEW). Management considers employee relations to be satisfactory. However, the Master Collective Bargaining Agreement with the IBEW, as amended, that governs the terms and conditions of employment for all IBEW represented employees working for the Company in the state of Alaska will expire on December 31, 2009. The Company expects to conduct extensive negotiations with the IBEW during 2009.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes

The Company utilizes the asset-liability method of accounting for income taxes in accordance with SFAS No. 109 *Accounting for Income Taxes*. Under the asset-liability method, deferred taxes reflect the temporary differences between the financial and tax basis of assets and liabilities using the enacted tax rates in effect in the years in which the differences are expected to reverse. Deferred tax assets are reduced by a valuation allowance to the extent that management believes it is more likely than not that such deferred tax assets will not be realized.

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation (FIN) 48, *Accounting for Uncertainty in Income Taxes*, which was effective for the Company on January 1, 2007. This Interpretation prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This Interpretation also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. The impact of the Company s reassessment of its tax positions in accordance with the adoption of FIN 48 did not have a material impact on the results of operations, financial condition or liquidity. The Company s policy is to recognize interest and penalties related to uncertain tax positions in income tax expense. As of December 31, 2008, the Company had no accrued income tax interest or penalties. Tax returns prior to 2005 are no longer subject to examination by major tax jurisdictions. The Company is not aware of any material tax contingencies.

Taxes Collected from Customers and Remitted to Government Authorities

The Company excludes taxes, collected from customers and payable to government authorities, from revenue. Taxes payable to government authorities are presented as a liability on the Consolidated Balance Sheets.

Regulatory Accounting and Regulation

The local telephone exchange operations of the Company account for costs in accordance with the accounting principles for regulated enterprises prescribed by SFAS No. 71. This accounting recognizes the economic effects of rate regulation by recording cost and a return on investment as such amounts are recovered through rates authorized by regulatory authorities. Accordingly, plant and equipment is depreciated over lives approved by regulators and certain costs and obligations are deferred based upon approvals received from regulators to permit recovery of such amounts in future years. The Company s cost studies and depreciation rates are subject to periodic audits that could result in reductions of revenues.

The Company utilizes blended depreciation rates for financial reporting, which management believes approximates the economical useful lives of the underlying plant. As a result, the Company has recorded a regulatory asset, as of December 31, 2008 and 2007, related to depreciation of the regulated telephone plant allocable to its intrastate and local jurisdictions. The balances at December 31, 2008 and 2007 are $63,363 and $65,271, respectively. The Company also has a regulatory liability of $64,117 and $62,443 at December 31, 2008 and 2007, respectively, related to accumulated removal costs for its local telephone subsidiaries. If the Company were not following SFAS No. 71, it would have followed SFAS No. 143, *Accounting for Asset Retirement Obligations* for asset retirement obligations associated with its regulated telephone plant. Non-regulated revenues and costs incurred by the local telephone exchange operations and non-regulated operations of the Company are not accounted for under SFAS No. 71 principles. In accordance with industry practice and regulatory requirements, revenue generated between regulated and non-regulated group companies are not eliminated on consolidation; these revenues totaled $41,597, $38,417 and $32,814 for the years ended December 31, 2008, 2007 and 2006, respectively.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

The local telephone exchange activities of the Company are subject to rate regulation by the FCC for interstate telecommunication service and the Regulatory Commission of Alaska (RCA) for intrastate and local exchange telecommunication service. The Company, as required by the FCC, accounts for such activity separately. Long distance services of the Company are subject to regulation as a non-dominant interexchange carrier by the FCC for interstate telecommunication services and the RCA for intrastate telecommunication services. Wireless, Internet and other non-common carrier services are not subject to rate regulation.

Non-Operating Expense

The Company periodically evaluates the fair value of its investments and other non-operating assets against their carrying value whenever market conditions indicate a change in that fair value. Any changes relating to declines in the fair value of non-operating assets are charged to non-operating expense under the caption Other in the Consolidated Statement of Operations.

Derivative Financial Instruments

The Company recognizes all derivatives as either assets or liabilities on the balance sheet and measures those instruments at fair value in accordance with SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, as amended. The accounting for changes in fair value of a derivative depends on the intended use of the derivative and its designation as a hedge. Derivatives that are not hedges are adjusted to fair value through earnings. If a derivative is a hedge, depending on the nature of the hedge, changes in fair value either offset the change in fair value of the hedged assets, liabilities or firm commitments through earnings, or are recognized in other comprehensive income until the hedged transaction is recognized in earnings. The change in a derivative s fair value related to the ineffective portion of a hedge, if any, is immediately recognized in earnings. The Company does not enter into any derivative contracts for speculative purposes. On the date a derivative contract is entered into, the Company designates the derivative as either a fair value or cash flow hedge. The Company formally assesses, both at the hedge s inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items. If the Company determines that a derivative is not highly effective as a hedge or that it has ceased to be a highly effective hedge, the Company would discontinue hedge accounting prospectively.

Dividend Policy

Dividends are payable when, as, and if declared by the Company s Board of Directors. In 2008, 2007 and 2006, the Company s board of directors declared quarterly cash dividends. Dividends on the Company s common stock are not cumulative.

Share-Based Payments

The Company accounts for share-based payments under SFAS No. 123(R), *Share-Based Payment*, which requires measurement of compensation cost from January 1, 2005, for all unvested stock-based awards at fair value on date of grant and recognition of compensation over the service period for awards expected to vest. The fair value for each stock option granted was estimated at the date of grant using a Black-Scholes option pricing model. Expected volatilities are based on historical volatilities of our common stock; the expected life represents the weighted average period of time that options granted are expected to be outstanding giving consideration to vesting schedules and our historical exercise patterns; the dividend yield is based on dividend yield of the option strike price at grant date; and the risk free interest rate on the grant date, for which the Company uses the lowest then effective Federal Funds interest rate stated by the Board of Governors of the Federal Reserve System. The Company determines the fair value of restricted stock based on the number of shares granted and the quoted market price of the Company s common stock on the date of grant, discounted for estimated dividend payments that do not accrue to the employee during the vesting period. Stock-based compensation is treated as a temporary difference for income tax purposes and increases deferred tax assets until the compensation is realized for income tax purposes. To the extent that the realized tax benefit

exceeds the book based compensation, the excess tax benefit is credited to additional paid in capital.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

In the second quarter of 2008, the Company granted performance stock units (PSUs) to certain executive employees contingent upon satisfaction of established performance goals. Compensation expense is recorded over the expected performance period, which is estimated by the Compensation Committee of the Company s Board of Directors. The Company re-measures the fair value of each PSU at each reporting period and records adjusted expense attributable to such period based on changes to the expected performance period or fair value of the Company s common stock or if the PSUs otherwise vest, expire, or are determined by the Compensation Committee to be unlikely to vest prior to expiration.

In September 2008, the Company began issuing stock-settled stock appreciation rights (SSARs) to certain of its executive officers. The Company computes the fair value of each SSAR at the date of grant using the same Black-Scholes pricing methodology that its uses to compute the fair value of a stock option on the Company s common stock.

Additionally, in the third quarter of 2008, the Company awarded restricted stock unit equivalents (RSUEs) to our Chief Executive Officer. These RSUEs are required to be settled in shares of the Company s common stock on a one-for-one basis on July 31, 2009, unless stockholder approval is not obtained, in which case they will be settled in cash. Compensation expense was recorded upon award and is adjusted at the close of each reporting period based upon the fair value of the Company s common stock until the RSUEs are converted to shares of common stock or paid in cash.

Accounting for Pensions

The Company accounts for pensions in accordance with FASB Statement No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans*. This statement requires an employer to recognize in its statement of financial position the over-funded or under-funded status of a defined benefit post-retirement plan measured as the difference between the fair value of a plan s assets and the benefit obligation. Employers must also recognize as a component of other comprehensive income, net of tax, the actuarial gains and losses and the prior service costs and credits that arise during the period. The adoption of the standard, effective December 31, 2006, had no impact as the plan is frozen.

On December 23, 2008, President Bush signed the Worker, Retiree, and Employer Recovery Act of 2008 (WRERA), which is designed to provide funding relief for certain defined benefit plans. Under the Pension Protection Act (PPA), and prior to enactment of WRERA, the Company was required to maintain a 92% funding level during 2008 to continue to qualify for transitional relief provided under the PPA. In the absence of any such transitional relief, any shortfall in funding below 100% would have been amortized and payable over a 7-year period. For most defined benefit plans, including the Company s single-employer plans, WRERA reduces the shortfall amount that is required to be amortized over a 7-year period to 92%, rather than 100%, for 2008. The Company is currently undertaking a review of WRERA to quantify its effect, if any, on the Company s obligation to make contributions during 2009.

Earnings per Share

The Company computes earnings per share based on the weighted number of shares of common stock and dilutive potential common share equivalents outstanding.

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

2. COMPONENTS OF ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

Components of accumulated other comprehensive income (loss) were comprised of the following:

	December 31,		
	2008	**2007**	**2006**
Minimum pension liability adjustment (1)	$ (6,700)	$ (2,855)	$ (4,188)
Tax effect of pension liability (2)	2,754	1,174	
Interest rate swap marked to fair value	(23,917)	(9,179)	5,754
Tax effect of interest rate swap (2)	9,833	3,773	
Total accumulated other comprehensive income (loss)	$ (18,030)	$ (7,087)	$ 1,566

(1) Liability adjustment is recorded pursuant to the Company s December 31, 2006, adoption of SFAS No. 158 *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans.*

(2) Tax effect is recorded pursuant to the 2007 release of the Tax Valuation Allowance. See Note 13 Income Taxes.

Components of other comprehensive income (loss) was comprised of the following:

	Year Ended December 31,		
	2008	**2007**	**2006**

Minimum pension liability adjustment	$ (3,845)	$ 1,333	$ 234
Tax effect of pension liability	1,580	1,174	
Interest rate swap marked to fair value	(14,738)	(14,933)	1,010
Tax effect of interest rate swap	6,060	3,773	
Total comprehensive income (loss)	$ (10,943)	$ (8,653)	$ 1,244

3. CREST COMMUNICATIONS ACQUISITION

Effective October 30, 2008, the Company closed its purchase of 100% of the outstanding stock of Crest Communications Corporation. The results of Crest s operations have been included in the Wireline segment of the Consolidated Financial Statements since that date. Crest s operations include an undersea fiber system of approximately 1,900 miles with cable landing facilities in Whittier, Juneau, and Valdez, Alaska and Nedonna Beach, Oregon. The system also includes terrestrial transport components linking Nedonna Beach, Oregon to the Network Operations Control Center in Hillsboro, Oregon and collocation facilities in Portland, Oregon and Seattle, Washington. The Company s management believes that the acquisition will complement the AKORN fiber build, by providing meaningful operating efficiencies and cost synergies, by offering enterprise customers the only diverse and redundant routing of traffic between Alaska and the lower 48, by allowing management the use of Network Operations Control Centers in Alaska and the lower 48, and by connecting our network to Southeast Alaska. Furthermore, management believes that the acquisition will drive incremental utilization of ACS differentiated Alaskan terrestrial assets from Crest s customer base and allow ACS to participate in the fast-growing bandwidth market ahead of AKORN s commercial launch.

The aggregate purchase price was $64,960, net of $1,072 in cash acquired and inclusive of $4,169 cash consideration that has been placed in an escrow account to be used for the settlement of any potential claims of misrepresentations, breach of warranties or covenants or for other indemnifications during the first eighteen months following the closing. The Company and Crest have made customary representations and warranties and covenants in the Agreement. Additionally, $4,000 has been deferred and placed in escrow until claims made by the Company against the selling stockholders for an unauthorized asset sale have been resolved.

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

3. CREST COMMUNICATIONS ACQUISITION (Continued)

A valuation of the business enterprise and acquired assets and liabilities was performed resulting in a determination that the fair value of the business enterprise was greater than the total acquisition price. The major asset acquired was the Northstar fiber network connecting Alaska with the lower 48, which was valued at replacement cost. In accordance with SFAS No. 141, *Business Combinations* (SFAS 141), the total cost of the acquisition has been allocated to the assets acquired and the liabilities assumed based on a pro-rata reduction of their estimated fair value at the date of acquisition. Certain purchase price adjustments are still under review and therefore the purchase price allocation is still subject to refinement. The following table summarizes the fair value of the assets acquired and liabilities assumed at the date of the acquisition after push-down of the excess.

		October 30, 2008
Current Assets	$	5,434
Property and equipment		61,685
Other assets		10
Deferred tax asset		3,393
Total assets acquired		70,522
Current liabilities		2,007
Long-term liabilities		2,483
Total liabilities assumed		4,490
Net assets acquired	$	66,032

4. FAIR VALUE MEASUREMENTS

The Company adopted the disclosure requirements of SFAS No. 157, *Fair Value Measurements* (SFAS No. 157) effective January 1, 2008. SFAS No. 157 clarifies the definition of fair value, prescribes methods for measuring fair value, establishes a fair value hierarchy based on the inputs used to measure fair value and expands disclosures about the use of fair value measurements. The valuation techniques required by SFAS No. 157 are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect internal market assumptions. These two types of inputs create the following fair value hierarchy:

Level 1- Quoted prices for identical instruments in active markets.

Level 2- Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable; and

Level 3 Significant inputs to the valuation model are unobservable. The fair values of cash and cash equivalents, accounts receivable and payable, and other short-term monetary assets and liabilities approximate carrying values due to their short-term nature.

Fair Value Measurements on a Recurring Basis

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurements. The Company s assessment of the significance of a particular input to the fair value measurements requires judgment, and may affect the valuation of the assets and liabilities being measured and their level within the fair value hierarchy.

The following table presents the balances of assets and liabilities measured at fair value on a recurring basis as of December 31, 2008 at each hierarchical level:

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

4. FAIR VALUE MEASUREMENTS (Continued)

		Fair Value Measurement at Reporting Date Using		
	Total	Quoted Prices in Active Markets for Identical Assets Level 1	Significant Other Observable Inputs Level 2	Significant Unobservable Inputs Level 3
Assets:				
Non-current investments	$ 1,005	$	$	$ 1,005
Liabilities:				
Other deferred credits and long-term liabilities	$ (23,917)	$	$ (23,917)	$

The following table presents the recociliation discoloures about fair value measurements at December 31, 2008 using significany unobservable (Level 3).

	Auction Rate Securities
Beginning balance, January 1, 2008	$
Total gains or losses (realized / unrealized) included in earnings	(245)
Purchases, issuances and settlements	1,250
Ending balance, December 31, 2008	$ 1,005
The amount of total gains or losses for the period included in earnings attributable to the change in unrealized gains or losses relating to assets still held at December 31, 2008	$ 245

Non-current investments consist of auction rate securities that have maturity dates greater than one year from December 31, 2008. The investments in auction rate securities are included in Level 3 as no active market or significant other observable inputs exist. The Company assigned a value to its ARS portfolio by reviewing the value assigned to similar securities by brokerages, relative yields, and assessing credit risk. An assessment was also done in which management determined that the securities were other-than-temporarily impaired, and in 2008, a charge was taken to the income statement of $245.

Included in liabilities, in other deferred credits and long-term liabilities, are derivative contracts, comprised of out-of-the-money interest rate swaps, that are valued using models based on readily observable market parameters for all substantial terms of the derivative contracts and thus are classified within Level 2.

Fair Value of Financial Instruments

The fair value of cash and cash equivalents, accounts receivable and payable, and other short-term monetary assets and liabilities approximate carrying value due their short-term nature. The fair value of the Company s 2005 senior credit facility, convertible notes, revolver draw, capital leases and other long-term obligations, of $443,358 and

$432,996, at December 31, 2008 and 2007, respectively, were estimated based on quoted market prices. Comparatively, the carrying values of these liabilities were $561,523 and $432,996 at December 31, 2008 and 2007, respectively.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

4. FAIR VALUE MEASUREMENTS (Continued)

Fair Value Measurements on a Nonrecurring Basis

In February 2008, the FASB issued Financial Statement of Position (FSP) SFAS 157-2, *Effective Date of FASB Statement No. 157*, which deferred the effective date of SFAS No. 157 for one year for certain non-financial assets and non-financial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis. In October 2008, the FASB also issued FSP SFAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active,* which clarifies the application of SFAS No. 157 in an inactive market and illustrates how an entity would determine fair value when the market for a financial asset is not active. On January 1, 2008, the Company adopted, without material impact on our consolidated financial statements, the provisions of SFAS No. 157 related to financial assets and liabilities and to non-financial assets and liabilities measured at fair value on a recurring basis. Beginning January 1, 2009, the Company will adopt the provisions required related to nonfinancial assets and non-financial liabilities that are not required or permitted to be measured at fair value on a recurring basis, which include those measured at fair value in goodwill impairment testing, indefinite-lived intangible assets measured at fair value for impairment assessment, non-financial long-lived assets measured at fair value for impairment assessment, asset retirement obligations initially measured at fair value, and those initially measured at fair value in a business combination. We do not expect the provisions of SFAS No. 157 related to these items to have a material impact on our consolidated financial statements.

SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of SFAS 115 (SFAS No. 159)

SFAS No. 159 permits but does not require the measurement of financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. As the Company did not elect to fair value any of our financial instruments under the provisions of SFAS No. 159, the adoption of this statement effective January 1, 2008 did not have an impact on the Company s financial statements.

5. ACCOUNTS RECEIVABLE

Accounts receivable trade consists of the following at December 31, 2008 and 2007:

	2008	2007
Customers	$ 30,420	$ 34,277
Connecting companies	8,460	6,901
Other	7,465	6,740
	46,345	47,918
Less: allowance for doubtful accounts	(5,912)	(8,768)
Accounts receivable trade, net	$ 40,433	$ 39,150

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

6. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consist of the following at December 31, 2008 and 2007:

	2008	2007
Land, buildings and support assets	$ 235,324	$ 204,858
Central office switching and transmission	344,532	332,528
Outside plant cable and wire facilities	585,288	524,925
Wireless switching and transmission	98,300	98,151
Other	2,822	6,022
Construction work in progress	125,085	42,773
	1,391,351	1,209,257
Less: accumulated depreciation and amortization	(891,899)	(825,663)
Property, plant and equipment, net	$ 499,452	$ 383,594

The following is a summary of property held under capital leases included in the above property, plant and equipment:

	2008	2007
Land, buildings and support assets	$ 17,665	$ 12,621
Outside plant cable and wire facilities	2,115	2,115
	19,780	14,736
Less: accumulated depreciation and amortization	(7,266)	(7,910)
Property held under capital leases, net	$ 12,514	$ 6,826

Amortization of assets under capital leases included in depreciation expense in 2008, 2007 and 2006 was $938, $1,189 and $1,205, respectively. Future minimum payments under these leases for the next five years and thereafter are as follows:

2009	$ 1,209
2010	1,212
2011	1,218
2012	1,217
2013	871
Thereafter	2,469
	$ 8,196

The Company leases various land, buildings, right-of-ways and personal property under operating lease agreements. Rental expense under operating leases for 2008, 2007 and 2006 was $7,559, $6,135 and $4,725, respectively.

Future minimum payments under these leases for the next five years and thereafter are as follows:

2009	$ 7,617
2010	6,901
2011	5,808
2012	5,332
2013	5,090
Thereafter	59,128
	$ 89,876

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

7. ASSET RETIREMENT

The Company accounts for asset retirement obligations in accordance with FIN No. 47, *Accounting for Conditional Asset Retirement Obligations*. FIN No. 47 requires the Company to recognize asset retirement obligations which are conditional on a future event. Uncertainty about the timing or settlement of the obligation is factored into the measurement of the liability. The Company has a regulatory asset and liability of $64,117 and $62,443 at December 31, 2008 and 2007, respectively, related to accumulated removal costs for its local telephone subsidiaries. Consistent with the industry, the Company follows SFAS No. 71 for asset retirement obligations associated with its regulated telephone plant. The Company s assets are pooled and the depreciable lives set by the regulators include a removal component which in effect accounts for the cost of removal. Non-regulated operations of the Company are accounted for under the principles of SFAS No. 143, *Accounting for Asset Retirement Obligations* and FIN No. 47 for which the Company has a retirement obligation of $1,969 and $1,411. These balances were recorded as a result of the Company s estimated obligation related to the removal of certain cell sites at the end of their operating lease term, adjusted for accretion/depreciation over the life of the lease. Also included in this balance is an acquired liability for $380, related to the removal of batteries in the Company s new cable operations.

The following table outlines the changes in the accumulated retirement obligation liability:

Balance, January 1, 2007	$ 1,171
Asset retirement obligation	143
Accretion expense	99
Settlement of lease obligations	(2)
Balance, December 31, 2007	$ 1,411
Asset retirement obligation	119
Accretion acquired	380
Accretion expense	117
Settlement of lease obligations	(58)
Ending Balance, December 31, 2008	$ 1,969

8. GOODWILL AND OTHER INTANGIBLE ASSETS

The Company performs its annual impairment test for goodwill in accordance with SFAS No. 142 *Goodwill and Other Intangible Assets*. The Company performs its annual impairment test as of the beginning of the fourth quarter or more frequently if events or changes in circumstance indicate possible impairment. The Company determines the fair value of each reporting unit for purposes of this test primarily by using a discounted cash flow valuation technique corroborated by comparative market multiples to determine the fair value of its businesses for comparison to their corresponding book values. Significant estimates used in the valuation include estimates of future cash flows, both future short-term and long-term growth rates, and estimated cost of capital for purposes of arriving at a discount factor. If the book value exceeds the estimated fair value for a reporting unit, a potential impairment is indicated and SFAS No. 142 prescribes the approach for determining the impairment amount, if any.

After conducting its 2008 test, the Company determined that goodwill attributable to its wireline operating segment was impaired resulting in an aggregate goodwill impairment charge of $29,553 that was recognized in the fourth quarter of 2008. The goodwill impairment charge is primarily driven by adverse equity market conditions, the industry transition from wireline to wireless products and services, decrease in current market multiples and the decline in the Company s stock price. This impairment charge reduces goodwill but does not impact the Company s overall business operations or cash flows. The tax benefit derived from recording the impairment charge was recorded

as a deferred income tax benefit and is included in the deferred tax assets as part of the net operating loss carry forwards. Prior to recording the goodwill impairment charges, the Company tested the amortizable intangible assets and other long-lived assets as required by SFAS No. 144, *Accounting for the Impairment or Disposal of Long-lived Assets*, and determined no impairment existed.

The Company also annually reassesses previously recognized intangible assets. Cellular and PCS licenses have terms of 10 years, but are renewable indefinitely through a routine process involving a nominal fee. The Company has determined that no legal, regulatory, contractual, competitive, economic or other factors currently exist that limit the useful life of its Cellular and PCS licenses. Therefore, the Company is not amortizing its Cellular and PCS licenses based on the determination

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Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

8. GOODWILL AND OTHER INTANGIBLE ASSETS (Continued)

that these assets have indefinite lives. The Company evaluates its determination of indefinite useful lives for its Cellular and PCS licenses each reporting period. Indefinite lived intangible assets are tested for impairment at least annually by comparing the fair value of the assets to their carrying amount. In 2008, the Company determined that the domain and trade names associated with its wireline segment were impaired and the balance of $88 was taken as an impairment loss.

Intangible assets with estimable useful lives are amortized over their respective estimated useful lives to their residual values and reviewed for impairment in accordance with the provisions of SFAS 144. The following table provides the gross carrying value and accumulated amortization for each major class of intangible asset by segment as of December 31, 2008 and 2007 based on the Company s reassessment of previously recognized intangible assets and their remaining amortization lives:

	Wireline	Wireless	Total
Goodwill:			
Balance, January 1, 2008	$ 29,553	$ 8,850	$ 38,403
Impairment loss	(29,553)		(29,553)
Balance, December 31, 2008	$	$ 8,850	$ 8,850
Indefinite-lived intangible assets:			
Domain names and trade names	$ 88	$	$ 88
Cellular licenses		18,193	$ 18,193
PCS licenses		3,323	3,323
Balance, January 1, 2008	$ 88	$ 21,516	$ 21,604
Spectrum licenses		$ 2,602	$ 2,602
Impairment loss	(88)		(88)
Balance, December 31, 2008	$	$ 24,118	$ 24,118

In 2007, the Company retired its only definite-lived intangible asset. This asset had a carrying value of zero at its retirement date. Amortization expense on that asset for the years ended December 31, 2008 and 2007 was zero and in 2006 was $91.

9. ACCOUNTS PAYABLE, ACCRUED AND OTHER CURRENT LIABILITIES

Accounts payable, accrued and other current liabilities consist of the following at December 31, 2008 and 2007:

	2008	2007
Accounts payable trade	$ 23,854	$ 19,160
Accrued payroll, benefits, and related liabilities	16,822	18,715
Dividend payable	9,449	9,226
Access revenue subject to refund	5,226	4,097
Unsettled acquisition costs	4,169	
Other	14,508	12,872

	$ 74,028	$ 64,070

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

10. LONG-TERM OBLIGATIONS

Long-term obligations consist of the following at December 31, 2008 and 2007:

	2008	2007
2005 senior credit facility term loan due 2012	$ 425,889	$ 427,900
5.75% convertible notes due 2013	125,000	
Revolving credit facility loan	5,000	
Capital leases and other long-term obligations	5,634	5,096
	561,523	432,996
Less current portion	(666)	(780)
Long-term obligations, net of current portion	$ 560,857	$ 432,216

The aggregate maturities of long-term obligations for each of the five years and thereafter subsequent to December 31, 2008 are as follows:

2009	$ 666
2010	737
2011	5,820
2012	551,792
2013	644
Thereafter	1,864
	$ 561,523

2005 Senior Credit Facility

During the first quarter of 2005, the Company completed refinancing transactions whereby it entered into a new $380,000 senior secured credit facility, the (2005 senior credit facility), which consisted of $335,000 of term loan borrowings and a $45,000 revolving loan facility.

On July 15, 2005, the Company completed a refinancing transaction whereby it amended and entered into a new term loan under its 2005 senior credit facility with substantially the same terms, increasing the size of the facility to $420,000. In February 2006, the Company amended its 2005 senior credit facility, increasing the $375,000 term loan under the facility by $52,900 and re-priced the facility to London Inter-Bank Offered Rate (LIBOR) plus 1.75% from LIBOR plus 2.00%. The amendment and the re-price became effective as of February 23, 2006 and February 22, 2006, respectively. The amendment permitted ACS Holdings to purchase any and all of its currently outstanding 9 7/8 % Senior Notes due 2011.

The $425,889 term loan balance under the 2005 senior credit facility was first drawn on February 1, 2005, and generally bears interest at an annual rate of LIBOR plus 1.75%, with a term of seven years from the date of closing and no scheduled principal payments before maturity. However, in conjunction with the new convertible debt offering in 2008, the Company paid down $2,011 of the term loan principal balance. At December 31, 2008 the Company had drawn $5,000 from its revolving credit facility leaving a remaining $40,000 un-drawn. To the extent drawn, the revolving credit facility bears interest at an annual rate of LIBOR plus 2.00% and has a term of six years from the date of closing. To the extent the $45,000 revolving credit facility under the 2005 senior credit facility is un-drawn, the Company will pay an annual commitment fee of 0.375% of the un-drawn principal amount over its term. The

Company also entered into floating-to-fixed interest rate swaps with total notional amounts of $135,000, $85,000, $40,000, $115,000 and $52,900, which swap the floating interest rate on the entire term loan borrowings under the 2005 senior credit facility for remaining periods at December 31, 2006 which range from one to three years, at a fixed rate of 5.88%, 6.25%, 6.18%, 6.71% and 6.75% per year, respectively, inclusive of the 1.75% premium over LIBOR. The swaps are accounted for as cash flow hedges.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

10. LONG-TERM OBLIGATIONS (Continued)

The 2005 senior secured credit facility contains a number of restrictive covenants and events of default, including covenants limiting capital expenditures, incurrence of debt and payment of dividends. The 2005 senior credit facility also requires that we achieve certain financial ratios quarterly and we are currently operating comfortably within these restrictions.

5.75% Convertible Notes due 2013

On April 8, 2008 the Company closed the sale of $125,000 aggregate principal amount of its 5.75% Convertible Notes due March 1, 2013. The notes were sold in a private placement pursuant to Rule 144A under the Securities Act of 1933. The Company received net proceeds from the offering of $110,053 after underwriter fees, the convertible note hedge, proceeds from the warrant and other associated costs.

The notes are unsecured obligations of the Company, subordinate to its obligations under its senior credit facility, will pay interest semi-annually in arrears on March 1 and September 1 of each year and will be convertible upon satisfaction of certain conditions. Upon conversion, holders will receive an amount in cash, shares of ACS common stock or a combination of both. The notes are guaranteed by substantially all of the Company s existing subsidiaries. Holders of the notes will have the right to require the Company to repurchase all or some of their notes at 100% of their principal, plus any accrued interest, upon the occurrence of certain events. The Company also entered into a registration rights agreement with the initial purchasers of the notes. Under the registration rights agreement, the Company is obligated under certain circumstances to file a shelf registration statement under the Securities Act related to the resale of the notes and the common stock issuable upon conversion of the notes. If such registration statement is required and is not filed, or does not become effective within specified time periods, the Company will be required to pay additional interest to holders of the notes.

Concurrent with the issuance of the notes, the Company entered into convertible note hedge transactions with an affiliate of one of the initial purchasers and certain other financial institutions for the purpose of reducing the potential dilution to common stockholders. If the Company is required to issue shares of its common stock upon conversion of the notes, the Company has the option of receiving up to 9,266 shares of its common stock when the price is between $12.90 and $16.42 per share upon conversion. The Company entered into warrant transactions with the same counterparties whereby the financial institutions have the option of receiving up to the same number of shares of the Company s common stock when the price exceeds $16.42 per share upon conversion. The convertible note hedge had a cost of $20,431 and has been accounted for as an equity transaction in accordance with Emerging Issues Task Force (EITF) No. 00-19, *Accounting for Derivative Financial Instruments Indexed to, and Potentially settled in, a Company s Own Stock.* Tax benefits of $1,056 were recorded for the twelve months ended December 31, 2008, as an offset to the hedge. All future tax benefits from the deduction related to the purchase of the call option, as part of the convertible note hedge transaction, will be recorded to additional paid in capital over the term of the hedge transaction. The Company received proceeds of $9,852 related to the sale of the warrants, which has also been classified as equity because they meet all of the equity classification criteria within EITF No. 00-19. Further, the Company expects the adoption of FSP APB 14-1 to increase the interest expense on the 5.75% Convertible Notes due 2013 recorded in the results of operations by an annual amount of approximately $6.5 million.

The call options purchased and warrants sold contemporaneously with the sale of the convertible notes are equity contracts that meet the paragraph 11(a) scope exception of SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*, and hence do not need to be marked-to-market through earnings. In addition, since the call option and warrant transactions are accounted for as equity transactions, the payment associated with the purchase of the call options and the proceeds received from the issuance of the warrants were recorded in additional paid in capital in stockholders equity as separate equity transactions.

Each $1,000 principal of the notes are convertible unto 77.5014 shares of the Company s common stock, which is the equivalent of $12.90 per share, subject to adjustment upon the occurrence of specified events set forth under the

terms of the note. Upon conversion, subject to certain covenants under its existing credit facility, the Company intends to pay the holders the cash value of the applicable number of shares of its common stock, up to the principal amount of the note.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

10. LONG-TERM OBLIGATIONS (Continued)

Amounts in excess of the principal balance may be paid in cash or in stock at the Company s option. Holders may convert their notes, at their option, at any time prior to the close of business on the business day immediately preceding the maturity date for the notes under the following circumstances:

(1) during any fiscal quarter after the fiscal quarter ended June 30, 2008 (and only during any such fiscal quarter), if the last reported sale price of our common stock for at least 20 trading days in the period of 30 consecutive trading days ending on the last trading day of the immediately preceding fiscal quarter is equal to or more than 130% of the conversion price of the notes on the applicable trading day;

(2) during the five scheduled trading day period after any five consecutive trading-day period (the measurement period) in which the trading price per $1,000 principal amount of the notes for each day of the measurement period was less than the 98.0% of the product of the last reported sale price of the Company s common stock and the conversion rate of the notes on each such day; or

(3) upon the occurrence of specified corporate transactions described in the indenture governing the notes.

In addition, holders may also convert their notes at their option at any time beginning on November 1, 2012, and ending at the close of business on the second scheduled trading day immediately preceding the maturity date for the notes, without regard to the foregoing circumstances.

Holders who convert their notes, in connection with a change of control, may be entitled to a make-whole premium in the form of an increase in the conversion rate. In addition, upon a change in control, liquidation, dissolution or de-listing, the holders of the notes may require the Company to repurchase for cash all or any portion of their notes for 100% of the principal amount plus accrued and unpaid interest. As of December 31, 2008, none of the conditions allowing holders of the notes to convert, or requiring the Company to repurchase the notes, had been met. The Company may not redeem the notes prior to maturity.

While it is the Company s intent to settle the principal portion of this debt in cash, under the provisions of, EITF No. 04-08, *The Effect of Convertible Instruments on Diluted Earnings per Share*, the Company must use the if converted method set forth in SFAS No. 128, *Earnings per Share,* in calculating the diluted earnings per share effect of the assumed conversion of our contingently convertible debt. Under the if converted method , the after tax effect of interest expense related to the convertible securities is added back to net income, and the convertible debt is assumed to have been converted in to common stock at the earlier of the debt issuance date or the beginning of the period.

Also in accordance with SFAS No. 128, the warrants sold in connection with the hedge transaction will have no impact on earnings per share until the Company s share price exceeds $16.42. Prior to exercise, the Company will include the effect of additional shares that may be issued using the treasury stock method. The call options purchased as part of the hedging transaction were anti-dilutive as of December 31, 2008 and, therefore, will have no effect on earnings per share.

Repurchased 9 7/8% Senior Unsecured Notes due 2011

In January and February 2006, the Company s subsidiary, ACS Holdings, repurchased $8,039 principal amount of its existing 9 7/8% senior unsecured notes due 2011 (CUSIP No. 011679AF4) at a weighted average premium of 9.7% over the par value. The Company incurred an early extinguishment of debt charge of $1,227 in connection with this transaction, inclusive of $778 in cash premiums. In February 2006, ACS Holdings commenced a cash tender offer for any and all of the $56,939 aggregate principal amount of outstanding 9 7/8% senior unsecured notes due 2011 issued by ACS Holdings. On February 23, 2006, the Company successfully repurchased $52,899 of the remaining $56,939 outstanding principal balance of these notes. The Company incurred an early extinguishment of debt charge of $8,423 in connection with this transaction, inclusive of $5,640 in cash premiums. On August 15, 2007, the Company successfully repurchased the remaining $4,040 outstanding principal balance of these notes. The Company incurred an early extinguishment of debt charge of $355 in connection with this transaction, inclusive of $199 in cash premiums.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

10. LONG-TERM OBLIGATIONS (Continued)

Capital Leases and Other Long-term Obligations

The Company has entered into various capital leases and other financing agreements totaling $5,634 and $5,096 with a weighted average interest rate of 10.16% and 9.94% at December 31, 2008 and 2007, respectively.

11. OTHER DEFERRED CREDITS AND LONG-TERM LIABILITIES

Deferred credits and other long-term liabilities consist of the following at December 31, 2008 and 2007:

	2008	2007
Regulatory liabilities accumulated removal costs	$ 64,117	$ 62,443
Interest rate swaps	23,917	9,179
Refundable access revenue	1,146	6,895
Pension liability	3,556	
Other deferred credits	5,957	3,558
	$ 98,693	$ 82,075

12. NON-OPERATING CHARGES

The Company periodically evaluates the fair value of its investments and other non-operating assets against their carrying value whenever market conditions indicate a change in that fair value. Any changes relating to declines in the fair value of non-operating assets are charged to non-operating expense under the caption Other in the Consolidated Statement of Operations .

13. INCOME TAXES

The following table includes a reconciliation of federal statutory tax at 35%, 35%, and 34%, respectively, to the recorded tax (expense) benefit, for the years ended December 31, 2008, 2007 and 2006, respectively.

	2008	2007	2006
Computed federal income taxes at the statutory rate	$ 5,824	$ (11,530)	$ (4,665)
(Increase) reduction in tax resulting from:			
State income taxes (net of federal benefit)	966	(2,254)	(799)
Excess compensation not allowed		(209)	(60)
Other	197	(183)	(771)
Rate change		3,361	
Stock-based compensation	(485)	(489)	747
Valuation allowance		122,498	5,105
Total income tax benefit (expense)	$ 6,502	$ 111,194	$ (443)

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

13. INCOME TAXES (Continued)

The Company files a consolidated federal income tax return. The income tax provision for the years ended December 31, 2008 and 2007 comprised of the following charges:

	2008	2007
Current:		
Federal income tax	$ 48	$ (1,103)
State income tax	9	(198)
Total current	57	(1,301)
Deferred:		
Federal income tax	4,966	(7,616)
State income tax	1,479	(2,387)
Change in valuation allowance		122,498
Total deferred	6,445	112,495
Total income tax benefit (expense)	$ 6,502	$ 111,194

The Company accounts for income taxes under the asset-liability method. Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company s deferred tax assets and liabilities are recorded at a combined federal and state effective rate of 41.1% as of December 31, 2008 and 2007, are as follows:

	2008	2007
Deferred tax assets:		
Current:		
Accrued compensation	$ 3,723	$ 5,053
Allowance for doubtful accounts	2,430	3,604
Net operating loss carry forwards	3,238	6,757
Fair value on interest rate swaps	9,833	3,773
Pension liability	410	145
Specific reserves	685	1,022
Self insurance accruals	665	682
Other	161	311
	21,145	21,347
Long-term:		
Net operating loss carry forwards	56,076	41,141
Alternative minimum tax carry forward	5,169	1,866
Intangibles/goodwill	25,782	20,428
Deferred revenue	865	

Pension liability	2,344	1,029
Property, plant and equipment	21,319	29,807
Stock-based compensation	3,125	1,732
Other	151	92
	114,831	96,095
Total deferred tax assets	$ 135,976	$ 117,442

In the year ended December 31, 2008, the Company generated a taxable loss which was primarily caused by electing to take bonus depreciation, as allowed under the Economic Stimulus Act of 2008 , on qualified fixed assets. Offsetting the loss, the Company recorded a tax benefit related to NOL s generated in the current year. In the year ended December 31, 2007 the Company recorded a net benefit when management reversed 100% of the existing valuation allowance. The allowance was reversed as management believed it was more likely than not that all of the deferred tax assets would be realized based on the weight of all available evidence, including two years of positive net income and projected future earnings. In 2008, if it

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

13. INCOME TAXES (Continued)

were not for the bonus depreciation taken for tax purposes and the goodwill write-off for book purposes the Company would have recorded income for both book and tax purposes. Therefore, management continues to believe that all of the deferred tax assets will be realized and the release of our valuation allowance was appropriate.

The Company files consolidated income tax returns with all if its subsidiaries for U.S. Federal purposes and with the States of Alaska and Oregon. The Company is no longer subject to examination for years prior to 2005. The Company is not currently being audited, nor has it been notified of any pending audits. The Company is not aware of any controversial or unsupported positions taken on its tax returns that have not either been resolved in prior audits, by amending prior returns or by adjusting its Net Operating Loss (NOL) carry forwards to rectify its filings. The Company has a $1,041 income tax receivable at December 31, 2008 and a $137 income tax payable at December 31, 2007.

The Company accounts for income tax uncertainties using the provision of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). The Company has reviewed all of its tax filings and position taken on its returns and has not identified any material current or future effect on its consolidated results of operations, cash flows or financial position.

In connection with the provisions of SFAS No. 123(R), the Company elected to calculate the pool of excess tax benefits under the modified retrospective method, but only to prior interim periods in the year of initial adoption. Future tax benefits increased $1,393 and decreased $1,011 in 2008 and 2007, respectively.

The Company has available at December 31, 2008, unused acquired and operating loss carry forwards of $148,002 federal and $120,057 state that may be applied against future taxable income as shown below:

	Federal			State
Year of Expiration	Acquired Unused Operating Loss Carry forwards	Unused Operating Loss Carry forwards	Total Unused Operating Loss Carry forwards	Total Unused Operating Loss Carry forwards
2018	$ 8,879	$	$ 8,879	$
2020	2,209		2,209	2,193
2021		34,034	34,034	30,719
2022	7,797	17,983	25,780	17,458
2023	4,565		4,565	
2024	230	43,974	44,204	43,715
2025		22,648	22,648	22,613
2026	2,299		2,299	
2028		3,384	3,384	3,359
	$ 25,979	$ 122,023	$ 148,002	$ 120,057

Acquired unused operating loss carry forwards associated with the Company s acquisition of Internet Alaska in June 2000 and Crest in October of 2008 are limited by Section 382 of the Internal Revenue Code of 1986. Internet Alaska is limited to $216 and Crest is limited to $3,068 per year plus the benefit of unrealized built-in gains. To the extent that these limits are not used they can be carried forward to subsequent years thereby effectively increasing that

year s limitation.

Section 382 of the Internal Revenue Code of 1986, as amended, imposes an annual limit on the ability of loss corporations that undergo an ownership change . This limitation restricts the amount of operating losses that can be used to reduce its future taxable income. On December 7, 2005 ACS underwent an ownership change thereby subjecting it to the Section 382 loss limitation rules. The corrected overall annual limitation at date of ownership change was $14,874 per year annually increased by unrealized built-in gains of $10,794. The increase in limitation will be in effect through the year

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

13. INCOME TAXES (Continued)

2010. The taxable loss generated in 2005 after the change in ownership from December 7, 2005 through the end of the year was $1,489 and has no limitations. In addition to the utilization of Internet Alaska s operating losses, ACS utilized additional operating losses of zero and $23,882 for 2008 and 2007, respectively, out of its operating loss carry forward.

14. EARNINGS PER SHARE

Earnings per share are based on weighted average number of shares of common stock and dilutive potential common shares equivalents outstanding. Basic earnings per share includes no dilution and is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution of securities that could share in the earnings of an entity. The Company includes dilutive stock options based on the treasury stock method. Due to the Company s reported net losses for the year ended December, 31, 2008, 1,428 potential common share equivalents, which consisted of options, restricted stock and stock-settled stock appreciation rights (SSARs) granted to employees and deferred shares granted to directors, were anti-dilutive. Also excluded from the calculation were shares related to the Company s convertible debt which were anti-dilutive for the twelve month period ending December 31, 2008. No shares were anti-dilutive at December 31, 2007 or December 31, 2006. The following table sets forth the computation of basic and diluted earnings per share for the years ending December 31, 2008, 2007 and 2006:

	2008	2007	2006
Numerator net income (loss)	$ (10,139)	$ 144,136	$ 13,278
Denominator weighted average shares outstanding:			
Basic shares	43,391	42,701	42,045
Dilutive impact of restricted stock, options and deferred shares		1,484	1,342
Dilutive shares	43,391	44,185	43,387
Earnings (loss) per share:			
Basic	$ (0.23)	$ 3.38	$ 0.32
Diluted	$ (0.23)	$ 3.26	$ 0.31

15. STOCK INCENTIVE PLANS

Under various plans, ACS Group, through the Compensation Committee of its Board of Directors, may grant stock options, restricted stock, stock appreciation rights and other awards to officers, employees and non-employee directors. At December 31, 2008, ACS Group has reserved a total of 11,560 (11.56 million) shares of authorized common stock for issuance under the plans. In general, options under the plans vest ratably over three, four or five years and the plans terminate in 10 years. After the plans terminate, all shares granted under the plan, prior to its termination, continue to vest under the terms of the grant when it was awarded.

Alaska Communications Systems Group, Inc. 1999 Stock Incentive Plan

ACS Group has reserved 8,660 shares under this plan, which was adopted by the Company in November 1999. At December 31, 2008, 10,769 equity instruments have been granted, 3,488 have been forfeited, 4,742 have been exercised, and 1,385 shares are available for grant under the plan.

In August 2005, the Company began granting restricted stock units in lieu of stock options as the primary equity-based incentive compensation for executive and non-union represented employees. The time-based restricted stock units have vesting terms that range from three to five years with equal annual vesting amounts. The performance-based restricted stock units generally cliff vest in five years and have accelerated vesting terms of one third per year if specified performance criteria are met. A long term incentive program (LTIP) also exists for executive management. LTIP awards

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

15. STOCK INCENTIVE PLANS (Continued)

are awarded annually and cliff vest in five years with accelerated vesting in three years if cumulative three year performance criteria are met.

In June 2008, the Company began granting performance share units (PSUs) to certain executives under the 1999 Stock Incentive Plan. These performance based awards expire on December 31, 2009 if their vesting terms have not been met. The PSUs are awarded on the condition that the participant remains employed or in the service of the Company from the date of the Agreement through the time of vesting. Compensation expense associated with outstanding performance share units is recorded over the estimated performance period which would likely result in the vesting of the awards. The amount of expense recorded each period is dependent upon our estimate of the number of shares that will ultimately be issued. As the ultimate payout of these awards is subject to the approval of the compensation committee, the awards are being re-measured at each reporting period end until such time as they are vested.

The Company also granted SSARs to Ms. Pelletier, the Company s Chief Executive Officer and another named executive officer during 2008. The SSARs have a term of five years and include ratable vesting through December 2011. The Company accounts for the SSARs in the same manner as options using a Black-Scholes model for valuation.

2003 Options for Officer Inducement Grant

During 2003, the Company s Board of Directors awarded 1,000 options as an inducement grant in hiring the Company s Chief Executive Officer. As of December 31, 2008, 800 options have been exercised/converted and 200 are currently outstanding.

2008 Restricted Stock Unit Equivalents for Officer Inducement Grant

In September 2008, the Company entered into an amended and restated employment agreement with Liane Pelletier, the Company s Chief Executive Officer. Under the agreement, the Company granted Ms. Pelletier 100 fully vested (RSUEs). These RSUEs are required to be settled in shares of the Company s common stock on a one-for-one basis on July 31, 2009, unless required stockholder approval is not obtained, in which case they will be settled in cash. When settled, the Company will pay cash dividend equivalents on any and all dividends declared on shares of the Company s common stock from September 1, 2008 through July 31, 2009. The Company currently accounts for these RSUEs as a liability, re-measured at each reporting period.

Alaska Communications Systems Group, Inc. 1999 Employee Stock Purchase Plan

This plan was adopted by ACS Group in November 1999 and will terminate December 31, 2009. The Company has reserved 1,550 shares under this plan. At December 31, 2008, 752 shares are available for issuance and sale. All ACS Group employees and all of the employees of designated subsidiaries generally will be eligible to participate in the purchase plan, other than employees whose customary employment is 20 hours or less per week, is not more than five months in a calendar year, or who are ineligible to participate due to restrictions under the Internal Revenue Code.

A participant in the purchase plan may authorize regular salary deductions up to a maximum of 15% and a minimum of 1% of base compensation. The fair market value of shares which may be purchased by any employee during any calendar year may not exceed $25. The amounts so deducted and contributed are applied to the purchase of shares of common stock at 85% of the lesser of the fair market value of such shares on the date of purchase or on the offering date for such offering period. The offering dates are January 1 and July 1 of each purchase plan year, and each offering period will consist of one six-month purchase period. The first offering period under the plan commenced on January 1, 2000. Shares are purchased on the open market or issued from authorized but unissued shares on behalf of participating employees on the last business days of June and December for each purchase plan year and each such participant has the rights of a stockholder with respect to such shares. During the year ended December 31, 2008, approximately 22% of eligible employees elected to participate in the plan.

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

15. STOCK INCENTIVE PLANS (Continued)

ACS Group, Inc. 1999 Non-Employee Director Stock Compensation Plan

This plan was adopted by ACS Group in November 1999. ACS Group has reserved 350 shares under this plan. At December 31, 2008, 233 shares have been awarded and 117 shares are available for grant under the plan. In 2007 and 2006, the plan required directors to receive not less than 50% of their annual retainer in the form of ACS Group s stock. Directors were permitted to elect up to 100% of their annual retainer in the form of ACS Group s stock. Beginning January 1, 2008 the plan was revised to require that Directors receive a portion of their annual retainer in the form of shares of ACS Group s stock. Directors are permitted to elect to receive up to 100% of their remaining annual retainer and meeting fees in the form of ACS Group s stock. Once a year, the Directors elect the method by which they receive their stock (issued or deferred). During the year ended December 31, 2008, 28 shares under the plan were awarded to directors, of which 11 were deferred until termination of service.

SFAS No. 123(R) Share-Based Payment

Total compensation cost for share-based payments was $9,477, $6,390 and $7,668 for the twelve months ended December 31, 2008, 2007 and 2006, respectively

The Company purchases, from shares reserved under the *Alaska Communications Systems Group, Inc. 1999 Stock Incentive Plan,* sufficient vested shares to cover employee payroll tax withholding requirements upon the vesting of restricted stock. From time to time, the Company also purchases sufficient vested shares to cover employee payroll tax withholding requirements at the aggregated exercise price upon exercise of options. Shares repurchased by the Company for this purpose are not reallocated to the share reserve set aside for future grants under the plan. The Company expects to repurchase approximately 180 shares in 2009. This amount is based upon an estimation of the number of shares of restricted stock awards expected to vest and options expected to be exercised during 2009.

Stock Options and Stock-Settled Stock Appreciation Rights

No options were granted for the twelve months ended December 31, 2008, 2007 and 2006. There were 775 SSARs granted for the twelve months ended December 31, 2008 and no SSARs granted for the same period in 2007 or 2006.

Restricted Stock Units and Performance Share Units

There were 846, 591 and 760 restricted stock grants for the twelve months ended December 31, 2008, 2007 and 2006, respectively. There were 263 PSUs awards for the period ended December 31, 2008 and no PSUs granted for the same period in 2007 or 2006. The following table describes the assumptions used for valuation of equity instruments awarded during the twelve months ended December 31, 2008, 2007 and 2006:

	2008	2007	2006
Stock Options:			
Risk free rate	0.25% - 2.00%		
Dividend yield	7.59%		
Expected volatility factor	33.88%		
Expected option life (years)	3.22		
Expected forfeiture rate			
Restricted stock:			
Risk free rate	0.25% -2.25%	4.25% - 5.25%	4.50% - 5.25%
Quarterly dividend	$ 0.215	$ 0.215	$ 0.215
Expected, per annum, forfeiture rate	0% - 4.47%	4.47%	4.47%

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

15. STOCK INCENTIVE PLANS (Continued)

Options and Restricted Stock Outstanding

Stock Options and SSARs

Proceeds from the exercise of stock options for the year ended December 31, 2008 were $848. The Company chose to remit $3,003 of these proceeds for payroll taxes in exchange for shares surrendered back to the Company. Information on outstanding options under the plan for the year ended December 31, 2008 is summarized as follows:

	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Life	Aggregate Intrinsic Value
Outstanding, January 1, 2008	1,160	$ 5.27		
Granted	775	11.33		
Exercised	(573)	4.70		
Canceled or expired	(12)	11.01		
Outstanding at December 31, 2008	1,350	8.94	4.69	$ 2,479
Exercisable at December 31, 2008	749	$ 8.43	4.68	1,729

Select information on equity instruments under the plan for the years ended December 31, 2008, 2007 and 2006 follows:

	Twelve Months Ended December 31,		
	2008	2007	2006
Weighted-average grant-date fair value of equity instruments granted	$ 5.87	$10.48	$ 9.81
Total fair value of shares vested during the period	$8,403	$5,273	$2,762
Total intrinsic value of options exercised	$4,260	$2,225	$2,927

Restricted Stock and PSU s

Restricted stock grants outstanding, all of which are non-vested at December 31, 2008, are as follows:

	Number of Shares	Weighted Average Fair Value
Outstanding at January 1, 2008	1,296	$11.07
Granted	846	9.91
Vested	(593)	10.19
Canceled or expired	(167)	11.39
Outstanding at December 31, 2008	1,382	$10.70

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

15. STOCK INCENTIVE PLANS (Continued)

Unamortized stock-based payment and the weighted average expense period at December 31, 2008, are as follows:

	Unamortized Expense	Average Period to Expense (years)
Stock options	$ 426	0.9
Restricted stock	5,953	2.6
	$ 6,379	2.5

16. RETIREMENT PLANS

Pension benefits for substantially all of the Company s employees are provided through the Alaska Electrical Pension Plan (AEPP). The Company pays a contractual hourly amount based on employee classification or base compensation. As a multi-employer defined benefit plan, the accumulated benefits and plan assets are not determined for or allocated separately to the individual employer. The Company s portion of the plan s pension cost for 2008, 2007 and 2006 was $11,548, $11,772 and $11,892, respectively.

The Company also provides a 401(k) retirement savings plan covering substantially all of its employees. The plan allows for discretionary contributions as determined by the Board of Directors, subject to Internal Revenue Code limitations. There was no matching contribution for 2008, 2007 or 2006.

The Company also has a separate defined benefit plan that covers certain employees previously employed by Century Telephone Enterprise, Inc. (CenturyTel Plan). This plan was transferred to the Company in connection with the acquisition of CenturyTel s Alaska properties. Existing plan assets and liabilities of the CenturyTel Plan were transferred to the ACS Retirement Plan on September 3, 1999. Accrued benefits under the ACS Retirement Plan were determined in accordance with the provisions of the CenturyTel Plan. Upon completion of the transfer to the Company, covered employees ceased to accrue benefits under the plan. On November 1, 2000, the ACS Retirement Plan was amended to conform early retirement reduction factors and various other terms to those provided by the AEPP. As a result of this amendment, prior service cost of $1,992 was recorded and is being amortized over the expected service life of the plan participants at the date of the amendment. The Company uses the traditional unit credit method for the determination of pension cost for financial reporting and funding purposes and complies with the funding requirements under the Employee Retirement Income Security Act of 1974 (ERISA). With the recent down turn in the economy, the plan is not adequately funded under ERISA at December 31, 2008. Management is currently assessing the timing and amount of a contribution that the Company will make during 2009, to regain required funding levels. Management is also estimating what additional contributions the Company may be required to make in subsequent years in the event the value of the plan s assets remains volatile or continue to decline. In September 2007, the Company funded $300 for the 2006 tax year. The Company made no contributions in 2008. The Company uses a December 31 measurement date for the plan.

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

16. RETIREMENT PLANS (Continued)

The following is a calculation of the funded status of the ACS Retirement Plan using beginning and ending balances for 2008 and 2007 for the projected benefit obligation and the plan assets:

	2008	2007
Change in benefit obligation:		
Benefit obligation at beginning of year	$ 12,883	$ 13,604
Interest cost	810	782
Actuarial gain	166	(769)
Benefits paid	(765)	(734)
Benefit obligation at end of year	13,094	12,883
Change in plan assets:		
Fair value of plan assets at beginning of year	13,311	12,713
Actual return on plan assets	(3,008)	1,032
Employer contribution		300
Benefits paid	(765)	(734)
Fair value of plan assets at end of year	9,538	13,311
Funded status	$ (3,556)	$ 428

The plans projected benefit obligation equals its accumulated benefit obligation. The 2008 liability balance of $3,556 is recorded on the balance sheet in other deferred credits and long-term liabilities while the 2007 asset balance of $428 is recorded in deferred charges and other assets.

The following table represents the net periodic pension expense for the ACS Retirement Plan for 2008, 2007 and 2006:

	2008	2007	2006
Interest cost	$ 810	$ 782	$ 762
Expected return on plan assets	(1,031)	(994)	(858)
Amortization of loss	157	322	444
Amortization of prior service cost	203	203	203
Net periodic pension expense	$ 139	$ 313	$ 551

In 2009, the Company expects amortization of prior service costs of $203 and amortization of net gains and losses of $793.

	2008	2007
Components of other comprehensive income/loss:		
Prior service cost	$ 332	$ 535

Net loss	6,368	2,320
	$ 6,700	$ 2,855

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

16. RETIREMENT PLANS (Continued)

The assumptions used to account for the plan as of December 31, 2008 and 2007 are as follows:

	2008	**2007**
Discount rate for benefit obligation	6.63%	6.49%
Discount rate for pension expense	6.49%	6.49%
Expected long-term rate of return on assets	8.00%	8.00%
Rate of compensation increase	0.00%	0.00%

The discount rates were calculated using a proprietary yield curve based on the top 30% of the universe of bonds included in the bond pool. The expected long-term rate of return on assets rate is the best estimate of future expected return for the asset pool, given the expected returns and allocation targets for the various classes of assets.

The plan s asset allocations at December 31, 2008 and 2007, by asset category are as follows:

Asset Category	**2008**	**2007**
Equity securities*	54%	63%
Debt securities*	46%	35%
Other/Cash	0%	2%
Total	100%	100%

* Note that mutual funds that may contain both stock and bonds may be included in these categories.

The fundamental investment objective of the plan is to generate a consistent total investment return sufficient to pay plan benefits to retired employees, while minimizing the long term cost to the Company. The long-term (10 year and beyond) plan asset growth objective is to achieve a rate of return that exceeds the actuarial interest assumption after fees and expenses.

Because of the Company s long-term investment objectives, the Plan administrator is directed to resist being reactive to short-term capital market developments and to maintain an asset mix that is continuously rebalanced to adhere to the plan investment mix guidelines. The Plan s investment goal is to protect the assets longer term purchasing power. The Plan s assets are managed in a manner that emphasizes a higher exposure to equity markets versus other asset classes. It is expected that such a strategy will provide a higher probability of meeting the plan s actuarial rate of return assumption over time.

Based on risk and return history for capital markets along with asset allocation risk and return projections, the following asset allocation guidelines were developed for the plan:

	Minimum	**Maximum**
Equity securities	40%	100%
Fixed income	20%	60%
Cash equivalents	0%	10%

The benefits expected to be paid in each of the next five years, and in the aggregate for the five fiscal years thereafter, are as follows:

2009	$ 850
2010	891
2011	916
2012	926
2013	955
2014-2018	5,115

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

16. RETIREMENT PLANS (Continued)

The Company also has a separate executive post retirement health benefit plan. The Alaska Communications Systems Executive Retiree Health Benefit Plan (The ACS Health Plan) was adopted by the Company in November 2001 and amended in October 2002. The ACS Health Plan covers a select group of former management employees. The ACS Health Plan provides a graded subsidy for medical, dental and vision coverage. The Compensation Committee of the Board of Directors decided to terminate The ACS Health Plan in January 2004. In February 2005, the Board adopted a resolution to exclude a former employee from the plan, causing a $90 decrease in the accumulated post retirement benefit. Three people qualified under the plan are eligible for future benefits, but the plan is closed to future participants.

The Company uses the projected unit credit method for the determination of post retirement health cost for financial reporting and funding purposes and complies with the funding requirements under ERISA. No contribution was made to The ACS Health Plan for 2008, 2007 or 2006, and no contribution is expected in 2009. The Company uses a December 31 measurement date for the plan.

The following is a calculation of the funded status and a reconciliation of the beginning and ending balances for 2008 and 2007 for the projected benefit obligation and the plan assets for The ACS Health Plan:

	2008	2007
Change in accumulated post-retirement benefit obligation:		
Accumulated post-retirement benefit obligation at beginning of the year	$ 176	$ 168
Interest cost	10	10
Actuarial gain	1	
Benefits paid	(7)	(2)
Accumulated post-retirement benefit obligation at end of the year	180	176
Change in plan assets:		
Fair value of plan assets at beginning of year	236	218
Actual return on plan assets	(26)	20
Benefits paid	(7)	(2)
Fair value of plan assets at end of year	203	236
Funded status	$ 23	$ 60

The following represents the net periodic post-retirement benefit expense for The ACS Health Plan for 2008, 2007 and 2006:

	2008	2007	2006
Interest cost	$ 10	$ 10	$ 10
Expected return on plan assets	(14)	(13)	(12)
Amortization of net gain	(4)	(5)	
Net periodic post-retirement benefit	$ (8)	$ (8)	$ (2)

The Company expects to incur no net periodic costs associated with this plan in 2009. The actuarial assumptions used to account for The ACS Health Plan as of December 31, 2008 and 2007 is an assumed discount rate of 5.75% and 6.00% for projected benefit obligation and an assumed discount rate of 6.00% and 5.89% for plan expense, respectively, and an expected long-term rate of return on plan assets of 6.00%. The discount rate is based on Moody s AA Corporate bonds. The expected long-term rate of return on assets is the best estimate of future expected return for the asset pool, given the expected returns and allocation targets for the various classes of assets.

For measurement purposes, the assumed annual rate of increase in health care costs for the next five years and thereafter, for both Pre-65 and Post-65 premiums, is 7.00%.

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

16. RETIREMENT PLANS (Continued)

Assumed health care cost trend rates have a significant effect on the amounts reported for The ACS Health Plan. A one percentage point change in assumed health care cost trend rates would have the following effects for 2008:

	+1%	-1%
Effect on total of service and interest cost components		(1)
Effect on accumulated postretirement benefit obligation	7	(9)

The ACS Health Plan s asset allocations at December 31, 2008 and 2007, by asset category, are as follows:

Asset Category	2008	2007
Equity securities*	19%	28%
Debt securities*	73%	66%
Other/Cash	8%	6%
Total	100%	100%

* Note that mutual funds that may contain both stock and bonds may be included in these categories.

The fundamental investment objective of the plan is to realize an annual total investment return consistent with the conservative risk tolerance plan dictated by the Company. The investment profile of the plan emphasizes liquidity and income, some capital stock investment and some fluctuation of investment return. It is anticipated that the investment manager will achieve this objective by investing the account s assets in mutual funds. The portfolio may hold common stock, fixed income securities, money market instruments and U.S. Treasury obligations.

Based on risk and return history for capital markets along with asset allocation risk and return projections, the following asset allocation guidelines were developed for the plan:

	Target
Equity securities	30%
Fixed income	60%
Other/cash	10%

The benefits expected to be paid in each of the next five years, and in the aggregate for the five fiscal years thereafter are as follows:

2009	$10
2010	16
2011	16
2012	16
2013	16
2014-2018	59

F-36

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

17. BUSINESS SEGMENTS

Our segments and their principal activities consist of the following:

Wireline Wireline provides communication services including voice, broadband and data, next generation IP network services, network access, long distance and other services to consumers, carriers, business and government customers.

Wireless Wireless products and services include voice and data products and other value added services and equipment sales.

The Company also incurs interest expense, interest income and other operating and non-operating income and expense at the corporate level which are not allocated to the business segments, nor are they evaluated by the chief operating decision maker in analyzing the performance of the business segments. These non-operating income and expense items are provided in the accompanying table under the caption All Other in order to assist the users of these financial statements in reconciling the operating results and total assets of the business segments to the consolidated financial statements. Common use assets are held at ACS Holdings and are allocated to the business segments based on operating revenue. In accordance with industry practice and regulatory requirements, affiliate revenue and expense between local telephone and all other segments is not eliminated on consolidation. The accounting policies of the segments are the same as those described in the summary of significant accounting policies.

The following table illustrates selected financial data for each segment as of and for the year ended December 31, 2008:

	Wireline	Wireless	All Other	Eliminations	Total
Operating revenues	$261,534	$143,606	$ 19,391	$(34,934)	$389,597
Intersegment revenue	54,411	2,729	19,391		76,531
Eliminated intersegment revenue	(15,506)	(37)	(19,391)		(34,934)
Depreciation and amortization	52,159	8,223	13,620		74,002
(Gain) loss on disposal of assets, net	775	(39)	14		750
Loss on impairment of goodwill and intangible assets	29,641				29,641
Operating income (loss)	(32,394)	42,423	5,103		15,132
Interest expense	2,065	504	(35,490)		(32,921)
Interest income	1		1,694		1,695
Income (loss) before income tax	(30,328)	42,913	(29,226)		(16,641)
Income tax (expense) benefit	3,408	(17,950)	21,044		6,502
Net income (loss)	(26,920)	24,964	(8,183)		(10,139)
Total assets	561,305	188,604	10,645	(3,216)	757,338
Capital expenditures	107,920	12,151	7,118		127,189

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

17. BUSINESS SEGMENTS (Continued)

The following table illustrates selected financial data for each segment as of and for the year ended December 31, 2007:

	Wireline	Wireless	All Other	Eliminations	Total
Operating revenues	$260,975	$137,566	$ 11,207	$(23,963)	$385,785
Intersegment revenue	48,569	2,604	11,207		62,380
Eliminated intersegment revenue	(12,710)	(46)	(11,207)		(23,963)
Depreciation and amortization	53,297	13,199	4,841		71,337
Loss on disposal of assets, net	110	12	126		248
Operating income	11,327	43,315	5,797		60,439
Interest expense	38	1,208	(29,632)		(28,386)
Loss on extinguishment of debt			(355)		(355)
Interest income	2		2,018		2,020
Income (loss) before income tax	10,729	44,522	(22,309)		32,942
Income tax (expense) benefit	(664)	(18,191)	130,049		111,194
Net income	10,065	26,331	107,740		144,136
Total assets	464,824	191,194	7,185		663,203
Capital expenditures	28,213	15,662	18,964		62,839

The following table illustrates selected financial data for each segment as of and for the year ended December 31, 2006:

	Wireline	Wireless	All Other	Eliminations	Total
Operating revenues	$242,601	$115,412	$ 10,687	$(19,979)	$348,721
Intersegment revenue	39,474	2,632	10,687		52,793
Eliminated intersegment revenue	(9,250)	(42)	(10,687)		(19,979)
Depreciation and amortization	53,181	11,515	4,400		69,096
Loss on disposal of assets, net	469	23	613		1,105
Operating income	1,489	37,140	4,992		43,621
Interest expense	(373)	426	(30,498)		(30,445)
Loss on extinguishment of debt			(9,650)		(9,650)
Interest income	1		1,834		1,835
Income (loss) before income tax	1,117	37,565	(24,961)		13,721
Income tax (expense) benefit	(3,821)	(15,578)	18,956		(443)
Net income (loss)	(2,704)	21,987	(6,005)		13,278
Total assets	404,502	146,611	5,103		556,216
Capital expenditures	39,094	14,771	6,154		60,019

18. ACCOUNTING FOR DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company uses derivative financial instruments to hedge variable interest rate debt to manage interest rate risk. To the extent that derivative financial instruments are outstanding as of a period end, the fair value of those instruments, represented by the estimated amount the Company would receive or pay to terminate the agreement, is reported on the balance sheet.

The Company is party to floating-to-fixed interest rate swaps with total notional amounts of $135,000 and $85,000, respectively, which swap the floating interest rate on a portion of the term loan borrowings under the 2005 senior credit facility for a five year term at a fixed rate of 6.13% and 6.50%, per year. The Company also entered into

a six year $40,000 notional amount fixed to floating swap arrangement, effectively fixing the rate on this portion of the term loan at 6.43% per year.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

18. ACCOUNTING FOR DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES (continued)

In February 2006, the Company and ACS Holdings executed $115,000 and $52,900 notional amount floating-to-fixed interest rate swap agreements related to its $375,000 term loan under its 2005 senior bank credit facility. The swaps effectively fix the LIBOR rate on $115,000 and $52,900 principal amount of senior bank credit facility at 6.71% and 6.75%. On December 31, 2008, 2007 and 2006 substantially all for the Company s swaps were effective. During 2008, in connection with the Company s issuance of its 5.75% convertible notes Due 2013, the Company prepaid $2,011 of principal required by its senior credit facility. The Company did not adjust its swap position to compensate for the prepayment as it was determined the overall effect on the hedge position was de minimus.

The negative carrying value of our swaps of $23,917, gross of $9,833 in tax, is the result of our fair value estimate at December 31, 2008. This balance was recorded as other comprehensive loss in the Company s Consolidated Statement of Stockholders Equity (Deficit) with a corresponding liability recorded in Other deferred credits and long-term liabilities on the Consolidated Balance Sheet.

Concurrent with the issuance of its 5.75% Convertible Notes due 2013, the Company entered into convertible note hedge transactions with an affiliate of one of the initial purchasers and certain other financial institutions for the purpose of reducing the potential dilution to common stockholders. If the Company is required to issue shares of its common stock upon conversion of the notes, the Company has the option of receiving up to 9,266 shares of its common stock when the price is between $12.90 and $16.42 per share upon conversion. The Company entered into warrant transactions with the same counterparties who have the option of receiving up to the same number of shares of the Company s common stock when the price exceeds $16.42 per share. The convertible note hedge had a cost of $20,431 and the Company received proceeds of $9,852 related to the sale of the warrants, each of which has been accounted for as an equity transaction in accordance with EITF No. 00-19.

19. COMMITMENTS AND CONTINGENCIES

The Company enters into purchase commitments with vendors in the ordinary course of business. The Company also has long-term purchase contracts with vendors to support the ongoing needs of its business. These purchase commitments and contracts have varying terms and in certain cases may require the Company to buy goods and services in the future at predetermined volumes and at fixed prices.

The Company is involved in various claims, legal actions and regulatory proceedings arising in the ordinary course of business and has recorded litigation reserves of $350 as of December 31, 2008 against certain current claims and legal actions. The Company believes that the disposition of these matters will not have a material adverse effect on the Company s consolidated financial position, results of operations or cash flows.

The Company pledges substantially all property, assets and revenue as collateral on its outstanding debt instruments.

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Notes to Consolidated Financial Statements, Continued
Years Ended December 31, 2008, 2007 and 2006
(In Thousands, Except Per Share Amounts)

20. SELECTED QUARTERLY FINANCIAL INFORMATION (unaudited)

	Quarterly Financial Data				
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Total
2008					
Operating revenues	$96,776	$94,356	$101,322	$ 97,143	$389,597
Operating income	16,908	9,699	12,121	(23,596)	15,132
Net income (loss)	5,776	908	2,044	(18,867)	(10,139)
Net income per share:					
Basic	0.13	0.02	0.05	(0.43)	(0.23)
Diluted	0.13	0.02	0.05	(0.43)	(0.23)
2007					
Operating revenues	$91,623	$94,501	$100,554	$ 99,107	$385,785
Operating income	14,157	13,351	17,886	15,045	60,439
Net income	7,312	6,169	10,300	120,355	144,136
Net income per share:					
Basic	0.17	0.14	0.24	2.81	3.38
Diluted	0.17	0.14	0.23	2.71	3.26

Table of Contents

ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.
Schedule II Valuation and Qualifying Accounts
(In Thousands)

Description	Balance at Beginning of Period	Charged to costs and expenses	Charged to other accounts (2)	Deductions (3)	Balance at End of Period
Year ended December 31, 2008					
Allowance for doubtful accounts	$ 8,768	$ 4,624	$ 105	$ (7,585)	$ 5,912
Valuation allowance for deferred taxes	$	$	$	$	$
Year ended December 31, 2007					
Allowance for doubtful accounts	$ 7,434	$ 5,103	$ 2	$ (3,771)	$ 8,768
Valuation allowance for deferred taxes	$122,498	$(122,498)(1)	$	$	$
Year ended December 31, 2006					
Allowance for doubtful accounts	$ 6,206	$ 5,121	$ (61)	$ (3,832)	$ 7,434
Valuation allowance for deferred taxes	$127,603	$ (5,105)(1)	$	$	$122,498

(1) Change in the valuation allowance allocated to income tax expense.

(2) Represents the reserve for accounts receivable collected on behalf of others, net of recovery.

(3) Represents credit losses, net of recovery.

F-41