INTER TEL INC
Form PREC14A
April 28, 2006

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
SCHEDULE 14A
(Rule 14a-101)
Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934

Filed by the Registrant þ
Filed by a Party other than the Registrant ¨
Check the appropriate box:

þ Preliminary Proxy Statement

¨ Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))

¨ Definitive Proxy Statement

¨ Definitive Additional Materials

¨ Soliciting Material Pursuant to §240.14a-11(c) or §240.14a-12

INTER-TEL, INCORPORATED
(Name of Registrant as Specified in Charter)
(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

þ No fee required.

¨ Fee computed on table below per Exchange Act Rules 14a-6(i)(4) and 0-11.

(1) Title of each class of securities to which transaction applies:

(2) Aggregate number of securities to which transaction applies:

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(4) Proposed maximum aggregate value of transaction:

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¨ Fee paid previously with preliminary materials.

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(1) Amount Previously Paid:

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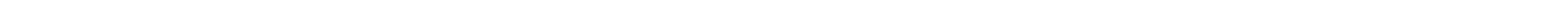

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INTER-TEL, INCORPORATED
NOTICE OF ANNUAL MEETING OF SHAREHOLDERS
May 31, 2006

TO THE SHAREHOLDERS:

NOTICE IS HEREBY GIVEN that the Annual Meeting of Shareholders of Inter-Tel, Incorporated (the ***Company***), an Arizona corporation, will be held on May 31, 2006, at 8:00 a.m., local time, at [*], Arizona 85226, for the following purposes:

1. To elect directors to serve for the ensuing year and until their successors are duly elected and qualified;
2. To approve the reincorporation of the Company into Delaware;
3. To approve a special resolution authorizing the Company s Board of Directors (sometime referred to below as the Board of Directors, the Board or the Inter-Tel Board) to effect an amendment to the Company s charter documents requiring the approval of a majority of disinterested shareholders to effect certain business combination transactions involving interested parties;
4. To consider and ratify the appointment of Ernst & Young LLP as the Company s independent registered public accounting firm; and
5. To consider and ratify a proposal to adjourn the Annual Meeting, if necessary, to solicit additional votes in favor of Proposals 1 through 4.

We will transact such other business as may properly come before the meeting or any adjournment thereof. In that connection, we have received notice from Mr. Steven G. Mihaylo, the former Chief Executive Officer of the Company (Mr. Mihaylo) that he intends to nominate three directors, including himself, for election to the Company s Board of Directors and to bring before the Annual Meeting the following additional proposals:

6. To urge the Company s Board of Directors to arrange for the prompt sale of the Company to the highest bidder;

7.-9. To repeal three specific recently-adopted amendments to the Company s Bylaws;

10. To amend the Company s Bylaws to require the unanimous vote of all members of the Company s Board to adopt any amendment to the Company s Bylaws that could have an anti-takeover effect;
11. To consider a resolution that each and every provision of the Company s Bylaws adopted by the Company s Board after March 29, 2006 and prior to the adoption of the resolution proposed in item 8 above be repealed.

Each of the foregoing items of business is more fully described in the Proxy Statement accompanying this Notice and will be discussed at the Annual Meeting with adequate time allotted for shareholder questions.

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Only shareholders of record at the close of business on March 22, 2006 (the ***Record Date***) are entitled to notice of and to vote at the meeting. A copy of the Company s 2005 Annual Report to Shareholders, which includes certified financial statements, will be mailed with this Notice and Proxy Statement on or about April [___], 2006 to all shareholders of record on the Record Date.

YOUR VOTE IS IMPORTANT, NO MATTER HOW MANY OR HOW FEW SHARES YOU OWN. PLEASE SIGN AND DATE THE ENCLOSED WHITE PROXY CARD AND RETURN IT IN THE ENCLOSED ENVELOPE PROMPTLY. PROPERLY VOTING THE ENCLOSED WHITE PROXY CARD AUTOMATICALLY REVOKES ANY PROXY PREVIOUSLY SIGNED OR RETURNED BY YOU.

DO NOT RETURN ANY BLUE PROXY CARD SENT TO YOU BY MR. MIHAYLO. Even if you have previously voted on Mr. Mihaylo s blue proxy card, you have every legal right to change your vote by signing, dating and returning the enclose WHITE Proxy Card. ONLY YOUR LATEST DATED PROXY WILL COUNT AT THE MEETING.

All shareholders are cordially invited to attend the meeting in person. However, to assure your representation at the meeting, you are urged to sign, date and return the White Proxy Card as promptly as possible in the postage-prepaid envelope provided. Any shareholder attending the meeting may vote in person even if he or she has previously returned a proxy. If you hold your shares through a bank, broker or other custodian, you must present a legal proxy from the record holder of your shares in order to vote at the meeting.

Sincerely,
KURT R. KNEIP, Secretary
Phoenix, Arizona
April [___], 2006

If you have questions or need assistance voting your shares,
please call the firm assisting the Company in the solicitation of proxies:

INNISFREE M&A INCORPORATED
Shareholders Call Toll Free: (888) 750 5834
Banks and Brokers Call Collect: (212) 750 5833.

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INTER-TEL, INCORPORATED
1615 S. 52nd Street
Tempe, Arizona 85281
PROXY STATEMENT
INFORMATION CONCERNING SOLICITATION AND VOTING

General

This Proxy Statement is furnished by Inter-Tel, Incorporated (***Inter-Tel*** or the ***Company***), for use at the Annual Meeting of Shareholders to be held May 31, 2006 at 8:00 a.m., local time or at any postponement or continuation of the meeting, as applicable, or at any adjournment thereof (as applicable, the ***Annual Meeting***), for the purposes set forth herein and in the accompanying Notice of Annual Meeting of Shareholders. The Annual Meeting will be held at [_*_] located at [_*_], Arizona 85226. These proxy solicitation materials were mailed on or about April [___], 2006 to all shareholders entitled to vote at the Annual Meeting.

Record Date and Share Ownership

Only shareholders of record at the close of business on the Record Date, or March 22, 2006, are entitled to notice of and to vote at the Annual Meeting. As of the Record Date, 26,386,651 shares of the Company s Common Stock were issued and outstanding.

Revocability of Proxies

The enclosed proxy is being solicited by the Board of Directors of the Company. Any proxy given pursuant to this solicitation may be revoked by the person giving it at any time before its use by delivering to the Company a written notice of revocation or a duly executed proxy bearing a later date, or by attending the Annual Meeting and voting in person. Attendance at the meeting will not, by itself, revoke a proxy.

Voting and Solicitation

Every shareholder voting at the Annual Meeting for the election of directors may either (i) cumulate such shareholder s votes and give one nominee for director a number of votes equal to (a) the number of directors to be elected (eight), multiplied by (b) the number of shares of the Company s Common Stock held by such shareholder; or (ii) distribute such shareholder s votes on the same principle among as many nominees for director as the shareholder thinks fit, provided that votes cannot be cast for more than eight nominees. However, no shareholder will be entitled to cumulate votes for any nominee unless such nominee s name has been placed in nomination in accordance with the Company s bylaws prior to the voting and such shareholder, or another shareholder, has given notice at the Annual Meeting prior to the voting for directors of the intention of such shareholder to cumulate such shareholder s votes.

If you choose to cumulate your votes, you will need to submit a proxy card or a ballot and make an explicit statement of your intent to cumulate your votes, either by so indicating in writing on the proxy card or by indicating in writing on your ballot when voting at the annual meeting. If you hold shares beneficially in street name and wish to cumulate votes, you should contact your broker, trustee or nominee. If you sign your proxy card or voting

instruction card with no further instructions, the proxy holders may cumulate and cast your votes in favor of the election of some or all of the applicable nominees in their sole discretion, except that none of your votes will be cast for any nominee as to whom you instruct that your votes be withheld.

Cumulative voting applies only to the election of directors. For all other matters, each share of common stock outstanding as of the close of business on the Record Date is entitled to one vote and one vote may be cast for each share of the Company s Common Stock held by a shareholder.

A quorum will be present if a majority of the votes entitled to be cast are present in person or by valid proxy. Directors will be elected by a plurality of votes cast; the eight persons receiving the highest number of votes shall be elected as the directors of the Company.

Proposal No. 2 with regard to the reincorporation of the Company into Delaware must be approved by an affirmative vote of a majority of the outstanding shares entitled to vote.

If Proposal No. 2 is approved, then Proposal No. 3 must be approved by the affirmative vote of a majority of the outstanding shares entitled to vote. If Proposal No. 2 is not approved, then Proposal No. 3 must be approved by the affirmative vote of a majority of the shares represented and voting at the Annual Meeting. Abstentions and broker non-votes resulting from a broker s inability to vote a client s shares on non-discretionary matters will have the same effect as votes against the approval of Proposal No. 2, and, if Proposal No. 2 is approved, the same will be true with respect to Proposal No. 3. If Proposal No. 2 is not approved, abstentions and broker non-votes resulting from a broker s inability to vote a client s shares on non-discretionary matters will have no effect on the outcome of the vote on Proposal No. 3.

All of the other proposals set forth herein, including Proposal Nos. 4, 5, 6, 7, 8, 9, 10 and 11 must be approved by the affirmative vote of a majority of the shares represented and voting at the Annual Meeting. Consequently, with respect to all such proposals, abstentions and Broker non-votes resulting from a broker s inability to vote a client s shares on non-discretionary matters will have no effect on the outcome of the vote on such proposals.

If the enclosed White Proxy Card is properly executed and returned to the Company in time to be voted at the Annual Meeting, it will be voted as specified on the proxy, unless it is properly revoked prior thereto. If no instructions are indicated with respect to certain proposals, the proxy will be voted with respect to such proposals as follows: FOR the nominees listed in Proposal 1, with such votes being cumulated at the sole discretion of the proxy holders; and FOR Proposals 2, 3, 4, 5 and AGAINST Proposals 6, 7, 8, 9, 10 and 11.

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It is the intent of the Company s proxy holders to retain discretionary authority to vote on matters presented to the meeting for which the Company did not have adequate notice pursuant to Rule 14a-4(c)(1).

The cost of this proxy solicitation will be borne by the Company, including preparation, assembly, printing and mailing of solicitation materials. As a result of the solicitation of proxies by Mr. Mihaylo, the Company s expenses related to the solicitation of proxies will exceed those normally spent for an annual meeting. We have retained Innisfree M&A Incorporated as our proxy solicitor, for a solicitation fee of up to $250,000 plus expenses. Innisfree M&A will employ approximately 75 people to solicit proxies from the Company s stockholders. In addition, the Company may reimburse brokerage firms and other persons representing beneficial owners of shares of the Company s Common Stock for expenses incurred in forwarding solicitation material to such beneficial owners. Although no precise estimate can be made at the present time, the Company currently estimates that the total expenditures relating to the proxy solicitation incurred by the Company will be approximately $[_*], which will be borne by the Company. Although solicitation of proxies will generally be made by mail, proxies also may be solicited by certain of the Company s directors, officers and regular employees, personally or by telephone, facsimile, or other electronic means without additional compensation. Annex E to this Proxy Statement sets forth certain information relating to directors, nominees, officers and other employees who will be soliciting proxies on the Company s behalf.

Deadline for Receipt of Shareholder Proposals

Proposals of shareholders of the Company that are intended to be presented by such shareholders at the annual meeting of the Company for the fiscal year ending December 31, 2006 must be received by the Company no later than [*] [*], 2007, in order to be included in the proxy statement and form of proxy relating to such meeting.

SEC rules also establish a different deadline for submission of shareholder proposals that are not intended to be included in the Company s proxy statement with respect to discretionary voting. The discretionary vote deadline for the 2006 Annual Meeting was April 8, 2006. Mr. Mihaylo submitted his proposals prior to that date. If a shareholder gives notice of such a proposal after the discretionary vote deadline, the Company s proxy holders will be allowed to use their discretionary voting authority to vote against the shareholder proposal when and if the proposal is raised at the Company s year 2007 Annual Meeting. Your Proxy when properly executed will be voted as directed or, if no direction is given, will be voted for each of proposals 1 through 5, against each of proposals 6 through 11, and in the discretion of the Company s proxy holders on such other matters as may properly come before the meeting or any adjournments or postponements thereof. The discretionary vote deadline for the 2007 Annual Meeting is [___], 2007, 45 calendar days prior to the anniversary of the mailing date of this proxy statement.

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Independent Auditors

The independent auditors of the Company for the fiscal year ended December 31, 2005 were Ernst & Young LLP. A representative of Ernst & Young LLP will attend the annual meeting for purposes of responding to appropriate questions.

Multiple Shareholders Sharing One Address

In some instances, we may deliver to multiple stockholders sharing a common address only one copy of this proxy statement and its attachments. If requested by phone or in writing, we will promptly provide a separate copy of the proxy statement and its attachments to a stockholder sharing an address with another stockholder. Requests by phone should be directed to our Corporate Secretary at (480) 449-8900, or to InnisFree M&A Incorporated at (888) 750-5834 (Shareholders call toll free) or (212) 750-5833 (Banks and Brokers call collect), and requests in writing should be sent to Inter-Tel, Incorporated, Attention: Corporate Secretary, 1615 S. 52nd Street, Tempe, Arizona 85281. Stockholders sharing an address who currently receive multiple copies and wish to receive only a single copy should contact their broker or send a signed, written request to us at the address above.

ELECTION OF DIRECTORS

(Proposal No. 1)

Nominees.

Eight (8) directors are to be elected at the Annual Meeting. All eight nominees named below are currently directors of the Company. In the event that any nominee of the Company becomes unavailable for any reason or if a vacancy should occur before election (which events are not currently anticipated by the Company), the shares represented by the enclosed proxy may be voted for such other person as may be determined by the holders of such proxy. In the event that additional persons are nominated for election as directors, the proxy holders intend to vote all proxies received by them cumulatively, in their discretion, in such a manner as to ensure the election of as many of the nominees listed below as possible. In such event, the specific nominees to be voted for will be determined by the proxy holders in their discretion. The term of office of each person elected as a director will continue until the next annual meeting and until his successor has been duly elected and qualified.

The names of the nominees and certain biographical information relating to the nominees are set forth below.

Name of Nominee	Age	Current Position	Director Since
Norman Stout	48	Director and Chief Executive Officer	2006
Alexander Cappello	50	Chairman of the Board	2005
J. Robert Anderson	69	Director	1997
Jerry W. Chapman	65	Director	1999
Gary D. Edens	64	Director	1994
Steven E. Karol	51	Director	2006
Robert Rodin	52	Director	2006
Agnieszka Winkler	60	Director	2005

MR. STOUT was appointed Chief Executive Officer and a member of Inter-Tel s Board of Directors on February 22, 2006. He began his tenure at Inter-Tel in 1994 as a director. Four years later, he resigned from the board and joined Inter-Tel as executive vice president, chief administrative officer and president of Inter-Tel Software and Services. Prior to joining Inter-Tel, Mr. Stout was Chief Operating Officer of Oldcastle Architectural Products and since 1996, Mr. Stout also had served as President of Oldcastle Architectural West. Mr. Stout held previous positions as President of Superlite Block; Chief Financial Officer and Chief Executive Officer (successively) of Boorhem-Fields, Inc. of Dallas, Texas; and as a Certified Public Accountant with Coopers & Lybrand. He currently serves on the board of directors of Hypercom Corporation, a public company headquartered in Phoenix, Arizona. Mr. Stout holds a Bachelor of Business Administration degree in Accounting from Texas A&M and an MBA from the University of Texas.

MR. CAPPELLO was elected as one of our directors in the April, 2005 annual meeting of shareholders, and to Chairman at the July, 2005 Board meeting. Since March 1996, Mr. Cappello has served as the Chairman and Chief Executive Officer of the Cappello Group, Inc., a global boutique merchant bank, which includes Cappello Capital Corp. (member SIPC-NASD). He has over thirty years experience in corporate management & finance, investment banking, merchant banking both in the U.S. and overseas. He is currently or has been a member of the board of directors of several companies and institutions including: University of Southern California (USC) Board of Trustees/President-Elect of the Board of Governors & Alumni Association, RAND Corporation-Center for Middle East Public Policy, Genius Products, Inc. (NASDAQ:GNPI), CytRx Pharmaceuticals, Inc. (NASDAQ: CYTR), and Swiss American Financial & Euro American Financial (Chairman). Mr. Cappello is a member of the Young Presidents Organization (YPO), where he has served as Chairman of the International Board from 2003-2005. He received a Bachelor of Science degree from the Marshall School of Business at USC in 1977 with honors. He has been a guest lecturer at the USC, UCLA, and Harvard Business Schools and is a contributing author of The New Investor Relations, being published by Bloomberg PRESS.

MR. ANDERSON has served as one of our directors since February 1997 and currently serves as the Chairman of our Compensation Committee. Mr. Anderson held various positions at Ford Motor Company from 1963 to 1983, serving as President of the Ford Motor Land Development Corporation from 1978 to 1983. He served as Senior Vice President, Chief Financial Officer and as a member of the board of directors of The Firestone Tire and Rubber Company from 1983 to 1989, and as Vice Chairman of Bridgestone/Firestone, Inc. from 1989 through 1991. He most recently served as Vice Chairman, Chief Financial Officer and as a member of the board of directors of the Grumman Corporation from 1991 to 1994. He currently serves on the boards of GenCorp, Inc. and B-G Corp. Mr. Anderson is currently semi-retired, and he is an active leader in various business, civic and philanthropic organizations.

MR. CHAPMAN was elected as one of our directors in December 1999 and previously served as one of our directors from 1989 to 1992. He currently serves as the Chairman of our Audit Committee. As a Certified Public Accountant, he served with a local accounting firm from 1963 through 1969, at which time he joined Ernst & Ernst, a predecessor entity of Ernst & Young LLP. He became a partner of Ernst & Young in 1977 and, until retiring from the firm in 1989, served as engagement partner on a wide variety of audit, assurance and consulting engagements. Additionally, he managed Ernst & Young s practices in Arizona as well as various offices in the adjoining southwest states from 1980 through 1989. He then operated his own consulting firm through 1992 and joined Arthur Andersen in 1993 as a partner specializing in providing business consulting services. He retired from Arthur Andersen in 1999. Mr. Chapman currently serves on the board of directors of CoBiz Inc., a public company headquartered in Denver, Colorado. Additionally, he provides services for a small number of clients requiring strategic and market-driven services.

MR. EDENS has served as one of our directors since October 1994 and currently serves as the Chairman of our Corporate Governance and Nominating Committee. He was an executive with Southern Broadcasting Company 1968-1982, Harte-Hanks Radio, Inc, chief executive officer, 1982-1984, and Edens Broadcasting, Inc., chairman and chief executive officer 1984-1994. Mr. Edens has served on a number of corporate boards, such as Great Western Bank and Citibank (Arizona), as well as holding leadership positions on the Radio Advertising Board,

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National Radio Broadcasters Association and Young Presidents   Organization. In 1998 he was chairman of the annual international financial seminar for Chief Executives Organization and World Presidents   Organization. Since 1994, he has been president of The Hanover Companies, Inc., a private investment firm. He holds a B.S. Degree in Business Administration from the University of North Carolina at Chapel Hill. In 2005 he participated in continuing education for directors at Harvard Business School.

MR. KAROL was elected as one of our directors in February 2006. Mr. Karol is founder, Managing Partner, and Chairman of HMK Enterprises, Inc. and Watermill Group, which consists of Watermill Ventures and Watermill Advisors. He has been an investor, operator, and advisor for almost thirty years. Through HMK and Watermill, he has owned and operated close to 50 companies and has built both into enterprises with over $1 billion in revenue on several occasions. Mr. Karol serves on several corporate boards including: Mooney Aircraft Company (OTC:MNYG.OB) (Chairman), StockerYale (NASDAQ: STKR), and J. Walter Company. He is also on several not-for-profit boards, including the Tufts University Board of Overseers for the School of Engineering (Chairman), the Vermont Academy Board of Trustees (Chairman), and The Brain Tumor Society (Chairman of Strategic Planning). He is a former International President of the Young Presidents   Organization where he held many positions throughout his twenty-six year relationship with the organization. He is a former trustee of the Boston Ballet and a former overseer of the Boston Symphony Orchestra. Mr. Karol received his Bachelor of Science degree from Tufts University in 1976. He completed the President s Program of Leadership at the Graduate School of Business Administration at Harvard University in 1997.

MR. RODIN who was elected as one of our directors in February 2006, is currently the Chairman and CEO of RDN Group; strategic advisors focused on corporate transitions, customer interface, sales and marketing, and supply chain management. Previously, Mr. Rodin was Chairman and CEO of eConnections, a provider of extended supply chain intelligence solutions, which he founded in 1999. From 1991 to 1999, he served as the CEO of Marshall Industries (NYSE:MI), a $1.8 billion industrial electronics distributor and supply chain management company. Marshall Industries was recognized as the   World s Number One Business to Business Website , by Advertising Age Magazine and Information Week Magazine highlighted Marshall Industries as the   World s Number One Company in the Use of Technology , Additionally, CIO Magazine recognized Mr. Rodin as one of the   Top 100 Leaders for the New Millennium . Following the sale of Marshall to Avnet (NYSE:AVT) in 1999, Mr. Rodin served as president of global supply chain management and electronic commerce solutions and as a member of the Avnet Global Managing Board. Mr. Rodin currently serves as director of Napster (NASDAQ: NAPS), director and Vice Chairman of CommerceNet and director of SM&A (NASDAQ: WINS). Mr. Rodin s best selling book,   Free, Perfect and Now: Connecting to the Three Insatiable Customer Demands , chronicles the radical transformation of Marshall Industries. The changes he led have been taught as case studies at Harvard Business School, Columbia, USC, MIT, and Stanford University.

MS. WINKLER was elected as one of our directors in the April 2005 annual meeting of shareholders. Ms. Winkler was the founder, Chairman and CEO of two companies, Winkler Advertising, founded in 1984, and TeamToolz, Inc., founded in 1999, both of which were acquired. She is currently founder and Chairman of The Winkler Group, a management consultancy specializing in marketing efficiency and effectiveness for Fortune 1000 companies.

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She has served on the board of directors of two NASDAQ companies, SuperCuts and RenoAir, and currently serves on the board of directors of IP Locks, Inc. and the Board of Trustees of Santa Clara University. In addition, she has served on the boards of numerous professional and civic institutions throughout her career and currently sits on the boards of the Committee of 200 Foundation and the Western Folklife Center. Winkler has a BA and an MA and received an MBA from Santa Clara University in 1981. A frequent keynote speaker on the subjects of marketing and branding at industry meetings globally, she is also the author of Warp Speed Branding: The Impact of Technology on Marketing, published by Wiley in the US, China and Turkey.

THE BOARD UNANIMOUSLY RECOMMENDS THAT THE SHAREHOLDERS VOTE FOR EACH NOMINEE LISTED ABOVE.

ON APRIL 21, 2006 STEVEN G. MIHAYLO, THE FORMER CHIEF EXECUTIVE OFFICER OF THE COMPANY TOGETHER WITH SUMMIT GROWTH MANAGEMENT, LLC, AN ENTITY THROUGH WHICH MR. MIHAYLO MAKES INVESTMENTS, SUBMITTED THEIR PRELIMINARY PROXY STATEMENT (THE MIHAYLO PROXY) TO THE SEC. IN THE MIHAYLO PROXY, MR. MIHAYLO SUBMITTED FOR SHAREHOLDER CONSIDERATION A NUMBER OF PROPOSALS AS WELL AS COMMENTED ON TWO OF THE PROPOSALS SUBMITTED BY THE BOARD OF DIRECTORS IN THE COMPANY S PRELIMINARY PROXY STATEMENT. PURSUANT TO THE MIHAYLO PROXY MR. MIHAYLO INTENDS TO NOMINATE HIMSELF AND TWO OTHER PERSONS SELECTED BY HIM AND TO SUPPORT THE ELECTION OF SUCH NOMINEES AT THE ANNUAL MEETING AND HAS SOLICITED YOUR PROXY FOR SUCH NOMINEES. THE TERM OF OFFICE OF EACH PERSON ELECTED AS A DIRECTOR SHALL CONTINUE UNTIL THE NEXT ANNUAL MEETING OF STOCKHOLDERS AND UNTIL THAT PERSON S SUCCESSOR HAS BEEN ELECTED.

THE BOARD OPPOSES THE NOMINEES OF MR. MIHAYLO AND STRONGLY RECOMMENDS THAT YOU REJECT MR. MIHAYLO S NOMINEES BY DISREGARDING SUCH SOLICITATION BY MR. MIHAYLO. WE URGE YOU TO SIGN AND DATE THE ENCLOSED WHITE PROXY CARD AND RETURN IT TODAY IN THE POSTAGE PAID ENVELOPE PROVIDED.

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TO APPROVE THE REINCORPORATION OF THE COMPANY IN DELAWARE
(Proposal No. 2)

The Board has approved a proposal to change the Company s state of incorporation from Arizona to Delaware (the ***Reincorporation***). The Board believes the Reincorporation to be in the best interests of the Company and its shareholders for several reasons, as more fully discussed below.

The Reincorporation will be effected by merging the Company into a newly formed Delaware company (the ***Delaware Company***). Shareholders are urged to read this section of the Proxy Statement carefully, including the related annexes referenced below and attached to this Proxy Statement, before voting on the Reincorporation. The following discussion summarizes material provisions of the Reincorporation. This summary is subject to and qualified in its entirety by the Agreement and Plan of Merger and Reincorporation (the ***Reincorporation Agreement***) that will be entered into by the Company and the Delaware Company in substantially the form attached hereto as Annex A, the Certificate of Incorporation of the Delaware Company (the ***Delaware Certificate***), in substantially the form attached hereto as Annex B, as altered to effect changes approved by the Company s shareholders in Proposal No. 3, if applicable, and the bylaws of the Delaware Company (the ***Delaware Bylaws***), in substantially the form attached hereto as Annex C. Copies of the Articles of Incorporation of the Company filed in Arizona, as amended to date (the ***Arizona Articles***), and the bylaws of the Company, as amended to date (the ***Arizona Bylaws***), are available for inspection at the principal office of the Company and copies will be sent to shareholders free of charge upon written request.

Mechanics of the Reincorporation

The Reincorporation will be effected by the merger of the Company with and into the Delaware Company, a wholly-owned subsidiary of the Company that will be incorporated under the Delaware General Corporation Law (***Delaware Law***) for purposes of the Reincorporation. The Company will disappear as a result of the merger, and the Delaware Company will be the surviving corporation and will continue to operate the business of the Company. Assuming approval by the shareholders of the Company (the ***Shareholders***), the Reincorporation will become effective as soon as practicable.

At the effective time of the Reincorporation (the ***Effective Time***), the Company will be governed by the Delaware Certificate, the Delaware Bylaws and Delaware Law. Although the Delaware Certificate and the Delaware Bylaws are patterned after the Arizona Articles and the Arizona Bylaws, they nevertheless include provisions that do not exist in the current Arizona Articles, Arizona Bylaws or under the Arizona Business Corporation Act (***Arizona Law***). See Certain Differences in Corporate Governance and Other Differences Between the Corporation Laws of Arizona and Delaware below. It is important to note that, if Proposal No. 3 is adopted and the additional provision described there is included to the Delaware Certificate, the additional provision would be an important difference between the current Arizona Articles and the Delaware Certificate as filed. The description that follows in this Proposal No. 2 refers to the

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documents and laws governing the Company, without discussing the adoption of or describing the terms of the additional provision described in Proposal No. 3.

In the event the Reincorporation is approved, upon effectiveness of the Reincorporation, (1) each outstanding share of Company Common Stock will automatically be converted into one share of Common Stock of the Delaware Company (the ***Delaware Company Common Stock***). In addition, each outstanding option to purchase shares of Company Common Stock will be converted into an option to purchase the same number of shares of the Delaware Company Common Stock with no other changes in the terms and conditions of such options. The Company s other employee benefit arrangements will be continued by the Delaware Company upon the terms and subject to the conditions then in effect.

CERTIFICATES FOR SHARES IN THE COMPANY WILL AUTOMATICALLY REPRESENT SHARES IN THE DELAWARE COMPANY UPON COMPLETION OF THE MERGER, AND SHAREHOLDERS WILL NOT BE REQUIRED TO EXCHANGE STOCK CERTIFICATES AS A RESULT OF THE REINCORPORATION.

The Reincorporation will not result in any change in the business, location, management, assets, liabilities or net worth of the Company, nor will it result in any change in location of Company employees, including the Company s management. The consolidated financial condition and results of operations of the Delaware Company immediately after consummation of the Reincorporation will be the same as those of the Company immediately prior to the consummation of the Reincorporation. The capitalization of the Company immediately after consummation of the Reincorporation will be the same as immediately prior to the consummation of the Reincorporation. In addition, upon the effectiveness of the Merger, the Board of the Delaware Company (the ***Delaware Company Board***) will consist of those persons elected to the current Board of the Company and the individuals serving as executive officers of the Company immediately prior to the Reincorporation will continue as executive officers of the Delaware Company. Upon effectiveness of the Reincorporation, the Delaware Company will be the successor in interest to the Company and the Shareholders will become stockholders of the Delaware Company (the ***Stockholders***).

The Reincorporation Agreement provides that the Board may abandon the reincorporation at any time prior to the Effective Time if the Board determines that the Reincorporation is inadvisable for any reason. For example, Delaware Law or Arizona Law may be changed to reduce the benefits that the Company hopes to achieve through the Reincorporation, or the costs of operating as a Delaware corporation may be increased, although the Company does not know of any such changes that are contemplated. The Reincorporation Agreement may be amended at any time prior to the Effective Time, either before or after the shareholders have voted to adopt the proposal subject to applicable law. The Company will re-solicit the shareholders approval of the Reincorporation if the terms of the Reincorporation Agreement are changed in any material respects.

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Principal Reasons for the Reincorporation; Recommendation

Predictability, Flexibility and Responsiveness to Corporate Needs. Delaware has adopted comprehensive and flexible corporate laws which are revised regularly to meet changing business circumstances. The Delaware Legislature is particularly sensitive to issues regarding corporate law and is especially responsive to developments in modern corporate law. In addition, Delaware offers a system of specialized chancery courts to deal with corporate law questions. These courts have developed considerable expertise in dealing with corporate issues as well as a substantial and influential body of case law construing Delaware s corporate law. In addition, the Delaware Secretary of State is particularly flexible, expert and responsive in its administration of the filings required for mergers, acquisitions and other corporate transactions. Delaware has become a preferred domicile for most major American corporations and Delaware law and administrative practices have become comparatively well-known and widely understood. As a result of these factors, it is anticipated that Delaware law will provide greater efficiency, predictability and flexibility in the Company s legal affairs than is presently available under Arizona law.

Directors and Officers. The Board believes that reincorporation under Delaware law will enhance the Company s ability to attract and retain qualified directors and officers as well as encourage directors and officers to continue to make independent decisions in good faith on behalf of the Company. The law of Delaware offers greater certainty and stability from the perspective of those who serve as corporate officers and directors. The intense competition that has characterized the communications products and services industry has greatly expanded the challenges and risks facing the directors and officers of companies within the communications products and services industry. To date, the Company has not experienced difficulty in retaining directors or officers. However, as a result of the significant potential liability and relatively small compensation associated with service as a director, the Company believes that the better understood, and comparatively stable corporate environment afforded by Delaware will enable it to compete more effectively with other public companies, most of which are incorporated in Delaware, in the recruitment of talented and experienced directors and officers.

The parameters of director and officer liability are more extensively addressed in Delaware court decisions and are therefore better defined and better understood than under Arizona law. The Board believes that reincorporation in Delaware will enhance the Company s ability to recruit and retain directors and officers in the future, while providing appropriate protection for shareholders from possible abuses by directors and officers. In this regard, it should be noted that directors personal liability is not, and cannot be, eliminated under Delaware law for intentional misconduct, bad faith conduct or any transaction from which the director derives an improper personal benefit.

Takeover Response. The Company currently has in place a limited number of measures designed to protect shareholder interests in the event of a hostile takeover attempt against the Company. The Company proposes to include similar measures in the charter and bylaws of the Delaware Company. These measures include a requirement that holders of a substantial percentage of voting stock act together to call a special meeting of shareholders, advance notice provisions for shareholder proposals or director nominations at an annual meeting of

shareholders, and the requirement that actions by written consent of shareholders be unanimous. Many of these measures have not been as fully tested in the Arizona courts as in the Delaware courts. As a result, Delaware law affords greater certainty that these measures will be interpreted, sustained and applied in accordance with the intentions of the Board. In general, Delaware case law provides a well developed body of law defining the proper duties and decision making process expected of a Board in evaluating potential and proposed corporate takeover offers and business combinations. The Board believes that these measures and related Delaware law will help the Board to protect the Company s corporate strategies, to consider fully any proposed takeover and alternatives, and, if appropriate, to negotiate terms that maximize the benefit to the Company s shareholders.

Other reasons for the Board s recommendation of the Reincorporation include the availability in Delaware of statutory protection for Stockholders against potentially unfair business combinations and a greater ability under Delaware Law for a corporation s Board to exercise influence over the timing of stockholder action. These aspects of Delaware Law are intended both to prevent any potential acquirors of control of the Company from using coercive or abusive takeover-related tactics and to encourage such acquirors to negotiate directly with the Board. The Board believes that the overall effect of the Reincorporation will be to enhance the Board s ability to consider all appropriate courses of action for the benefit of all Shareholders and to negotiate effectively on their behalf in the context of a takeover attempt, thereby maximizing the benefits of any takeover for all Stockholders.

The Company is not seeking through this Proposal No. 2 to change the current charter and bylaw provisions of the Company and, except for those changes resulting from differences between Arizona and Delaware law, this Proposal No. 2 does not seek to alter the rights of the Company s shareholders or the rules by which the Company operates or by which its affairs are governed. The Board recommends that shareholders vote in favor of the Reincorporation.

As described in Proposal No. 3 in this proxy statement, the Board also is recommending that the shareholders approve changes to the Company s charter to impose a requirement of a majority approval of disinterested shareholders of any business combination involving the Company and an interested shareholder. The approval of Proposal No. 3 is to be considered and approved separately from the Reincorporation. You may vote in favor of the Reincorporation whether or not you choose to vote in favor of Proposals No. 3.

Possible Negative Considerations

Notwithstanding the belief of the Board as to the benefits to the Shareholders of the Reincorporation, some Shareholders may find the proposal disadvantageous to the extent it has the effect of discouraging a future attempt to acquire control of the Delaware Company that is not presented to and approved by the Delaware Company Board, but that a substantial number and perhaps even a majority of the Stockholders might believe to be in their best interests or in which Stockholders might receive a substantial premium for their shares over then current market prices. As a result of such effects, Stockholders who might desire to participate in such a transaction may not have an opportunity to do so. In addition, unapproved tender offers and takeover attempts may be made at times and in circumstances that are beneficial to and in the

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interests of certain Stockholders. Furthermore, a negotiated transaction is not necessarily more advantageous to the Stockholders than a non-negotiated transaction.

In addition, franchise taxes in Delaware will be greater than in Arizona. See below for a comparison of shareholders /stockholders rights and powers of management and under Delaware and Arizona law.

The Board has considered the potential disadvantages of the Reincorporation and has concluded that the potential benefits outweigh the possible disadvantages.

Differences Between the Corporation Laws of Arizona and Delaware

In general, the Company s corporate affairs are governed at present by Arizona Law as well as the Arizona Articles and the Arizona Bylaws, which have been adopted pursuant to Arizona law. As noted above, if the Reincorporation is effected, the Company will merge into, and its business will be continued by, the Delaware Company. Following the merger, issues of corporate governance and control would be controlled by Delaware, rather than Arizona Law and by the Arizona Articles and Arizona Bylaws, will, in effect, be replaced by the Delaware Certificate and the Delaware Bylaws. Accordingly, the differences among these documents and between Delaware and Arizona law are relevant to your decision whether to approve the reincorporation proposal.

Provisions of Arizona Law and Delaware Law differ in certain respects, and it is not practical to summarize all differences here. A summary of the material differences that may affect the rights and interests of Stockholders in the Delaware Company, however, is set forth below.

Indemnification and Limitation of Liability. Arizona Law provides that a corporation may indemnify a director or officer of the corporation, or a person who was serving at the corporation s request as a director, officer, partner, trustee, employee or agent of another enterprise or employee benefit plan, provided that the person (a) acted in good faith, (b) reasonably believed, in the case of conduct in his official capacity with the corporation, that the conduct was in the best interest of the corporation and, in all other cases, that his conduct was at least not opposed to the corporation s best interests, and (c) in the case of criminal proceedings, had no reasonable cause to believe the conduct was unlawful. No indemnification of an officer or director may be made in connection with a proceeding (i) by or in the right of the corporation in which the person has been adjudged to be liable to the corporation, or (ii) in connection with any other proceeding in which the person was adjudged liable on the basis that a financial benefit was improperly received by such a person.

Under Arizona Law, to the extent that an officer or director has been successful in the defense of the proceeding, he must be indemnified by the corporation for reasonable expenses incurred in connection with the proceeding. Unless otherwise limited by a company s articles of incorporation or Arizona Law, an outside director must be indemnified against liability, Expenses must be paid in advance of the final disposition of a suit upon receipt of the claimant s written affirmation of good faith belief that he has met the statutory standard of conduct and undertaking to repay such amount if it is ultimately determined that he did not

meet the statutory standard of conduct. Special rules apply to outside directors who are neither officers, directors nor 5% stockholders. Unless a court has determined before payment that an outside director failed to meet the statutory standard of conduct, an outside director must be indemnified against liability and his expenses must be paid in advance of a final disposition upon receipt from such outside director of a written affirmation of his good faith belief that he has met the statutory standard of conduct and an undertaking to repay the advance if it is ultimately determined that he did not meet such standard.

Unless mandatory indemnification applies, indemnification may be made under Arizona Law only upon determination that the person has met the statutory standard of conduct. This determination is made by (i) a majority vote of the directors not at the time parties to the proceeding, (ii) special legal counsel selected by majority vote of the disinterested directors, or, if there are no disinterested directors, by majority vote of the board, or (iii) by the shareholders, provided that shares owned by or voted under the control of directors who are at the time parties to the proceeding shall not be voted on the determination. Arizona Law does not limit a corporation s power to further indemnify and advance expenses to employees, agents or officers who are not acting as directors, provided that in the case of such officers, indemnification may not be provided for (x) liability in connection with a proceeding by or in the right of the corporation other than for reasonable expenses incurred in connection with the proceeding and (y) liability arising out of conduct that constitutes receipt by the officer of a financial benefit to which the officer is not entitled, an intentional infliction of harm on the corporation or shareholders, or an intentional violation of criminal law.

Delaware Law permits a corporation to include a provision in its certificate of incorporation, which is included in the Delaware Certificate, which eliminates or limits the personal liability of a director to the corporation or its shareholders for monetary damages for breach of fiduciary duty. However, no such provision may eliminate or limit director monetary liability for: (a) breaches of the director s duty of loyalty to the corporation or its stockholder; (b) acts or omissions not in good faith or involving intentional misconduct or knowing violations of law; (c) the payment of unlawful dividends or unlawful stock repurchases or redemptions; or (d) transactions in which the director received an improper personal benefit. Under Delaware Law, a corporation has the power to indemnify its directors, officers, employees and agents against judgments, settlements, and expenses in any litigation or other proceeding, except a proceeding by, or in the right of, the corporation, if the person acted in good faith and in a manner he or she reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to a criminal proceeding, had no reasonable cause to believe his or her conduct was unlawful. The indemnification provisions of Delaware Law require indemnification of a present or former director or officer to the extent that he has been successful on the merits or otherwise in defense of any action or claim. Delaware law also permits indemnification of expenses in a suit by, or in the right of, the corporation if the person acted in good faith and in a manner he or she reasonably believed to be in or not opposed to the best interests of the corporation, subject to court approval if the person is adjudged liable. The Delaware Certificate and the Delaware Bylaws generally require the Delaware Company to indemnify and advance litigation expenses to its directors and officers to the extent permitted by Delaware Law.

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Cumulative Voting for Directors. Cumulative voting permits the holder of each share of stock entitled to vote in the election of directors to cast that number of votes which equal the number of directors to be elected. The holder may allocate all votes represented by a share to a single candidate or may allocate those votes among as many candidates as he chooses. Thus, a shareholder with a significant minority percentage of the outstanding shares may be able to elect one or more directors if voting is cumulative.

Under Arizona Law cumulative voting in the election of directors is mandatory. Cumulative voting generally is not available under Delaware Law and is only available if so provided in the corporation s certificate of incorporation. In order to establish for Stockholders of the Delaware Company a set of rights approximating as closely as possible the rights of the Company s Shareholders, the Delaware Certificate so provides for cumulative voting.

Number of Directors. Arizona Law requires corporations to have at least one director but allows the number of persons constituting the Board of a corporation to be fixed by the bylaws or the articles of incorporation, and permits the bylaws to provide that the number of directors may vary within a specified range, with the exact number to be determined by the Board.

Delaware Law allows the number of persons constituting the Board of a corporation to be fixed by the certificate of incorporation or the bylaws, or fixed in the manner provided in the bylaws. The Delaware Certificate and Bylaws provide that the number of directors shall be determined from time to time exclusively by resolution of the Board.

The Arizona Bylaws fix the number of directors at nine, or such other number fixed by resolution of the Board. Presently, by virtue of such resolutions, the number of directors is eight. The Delaware Bylaws fix the number of directors at eight, or such other number fixed by resolution of the Board. Accordingly, despite the technical difference in the Delaware Bylaws, there will be no change in the number of directors if the Delaware Bylaws are adopted pursuant to the approval of this proposal.

Classified Board. Arizona Law and Delaware Law permit, but do not require, the adoption of a classified Board with staggered terms. Neither the Arizona Articles or Bylaws, nor the Delaware Certificate or Delaware Bylaws provide for a classified Board.

Removal of Directors. Under Arizona Law, a director may be removed with or without cause, unless the articles of incorporation provide that they may be removed only for cause, by the affirmative vote of a majority of the outstanding shares. A director may not be removed, however, if the number of votes sufficient to elect the director by cumulative voting is voted against removal of the director. The Arizona Articles do not provide that directors may be removed only for cause.

Delaware Law provides that any director or the entire board may be removed, with or without cause, by the holders of a majority of the shares then entitled to vote at an election of directors, except as follows: (i) unless the certificate of incorporation otherwise provides, in the case of a corporation where the board is classified, stockholders may effect such removal only

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for cause; or (ii) in the case of a corporation having cumulative voting, if less than the entire board is to be removed, no director may be removed without cause if the votes cast against such director s removal would be sufficient to elect such director if then cumulatively voted at an election of the entire Board if there are classes of directors or at an election of the class of directors of which such director is a part.

Neither the Arizona Articles nor the Delaware Certificate provide that directors may be removed only for cause.

Vacancies on the Board of Directors. Under Arizona Law, unless the articles of incorporation provide otherwise, if a vacancy occurs on a board of directors, including a vacancy resulting from an increase in the number of directors, either (i) the shareholders may fill the vacancy, (ii) the board of directors may fill the vacancy, or (iii) if the directors remaining in office constitute fewer than a quorum of the board, they may fill the vacancy by the affirmative vote of a majority of all of the directors remaining in office. If the vacant position was held by a director elected by a voting group of shareholders, only the holders of shares of that voting group are entitled to vote to fill the vacancy if it is filled by the shareholders. If at any time by reason of death or resignation or other cause a corporation has no directors in office, any officer or any shareholder may call a special meeting of shareholders for the purpose of electing directors.

Under Delaware Law, unless otherwise provided in the certificate of incorporation or bylaws, vacancies on the board of directors and newly created directorships resulting from any increase in the authorized number of directors may be filled by the vote of a majority of directors then in office, even though less than a quorum. Delaware Law also provides that where directors are elected by classes or series of stock, vacancies are to be filled by the remaining directors elected by the class or series in whose directorships the vacancy occurs. The Delaware Certificate and Bylaws provide that newly created directorships resulting from any increase in the authorized number of directors or any vacancies in the Delaware Company Board for any other reason may be filled only by a majority vote of the directors then in office, although less than a quorum, or by a sole remaining director. A director elected to fill a vacancy shall be elected to hold office until the next election of directors, subject to the election and qualification of his or her successor and to his or her earlier death, resignation or removal.

Shareholder Power to Call Special Meeting. Under Delaware Law, a special meeting of stockholders may be called by the Board or by any other person(s) authorized to do so in the certificate of incorporation or the bylaws. Under Arizona Law a special meeting of shareholders may be called by the Board or the person or persons authorized to do so by the articles of incorporation or bylaws. Arizona Law further provides that special meetings of the shareholders of issuing public corporations may be called by (i) the president, (ii) the secretary, (iii) two or more directors, (iv) a person authorized in the articles of incorporation or bylaws, or (v) a shareholder or shareholders holding ten percent or more of the voting power of all shares, except that a special meeting for the purpose of considering any action to directly or indirectly facilitate or effect a business combination, including any action to change or otherwise affect the composition of the Board for that purpose, must be called by twenty-five percent or more of the voting power of all shares.

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Both the Delaware and the Arizona Bylaws authorize the parties listed in (i) through (v) above to call special meetings of shareholders. Both the Arizona Bylaws and Delaware Bylaws provide that any request for a special meeting shall state the purpose or purposes of the proposed meeting and, if submitted by holder of less than twenty-five percent (25%) in amount of the entire capital stock of the Corporation, shall be accompanied by a declaration under penalty of perjury that the meeting is not being held for the purpose of considering any action to directly or indirectly facilitate a business combination , including any action to change or otherwise affect the composition of the Board for that purpose.

Actions by Written Consent of Shareholders. Under Arizona Law and Delaware Law, shareholders may execute an action by written consent in lieu of a shareholder meeting. Arizona law provides that action by written consent is permitted so long as all of the shares outstanding and entitled to vote on the matter provide consent in writing. Delaware Law permits a corporation to eliminate actions by written consent in its certificate of incorporation.

Both the Arizona Bylaws and Delaware Bylaws provide that written consent is permitted if signed by the holders of all of the shares of outstanding stock entitled to vote with respect to the subject matter of the action.

Advance Notice Requirement for Shareholder Proposals and Director Nominations. There is no specific statutory requirement under either Arizona Law or Delaware Law with regard to advance notice of director nominations and shareholder proposals. However, both the Arizona and the Delaware Bylaws provide that, in order for a shareholder to propose business to be conducted or to nominate directors for election at an annual meeting of shareholders, such shareholder must provide notice to the Company not less than ninety (90) days prior to the anniversary date of the immediately preceding annual meeting; provided, however, that in the event the annual meeting is called for a date that is not within thirty (30) days before or after such anniversary date, notice by the shareholder must be so received not later than the close of business on the tenth (10th) day following the day on which such notice of the date of the meeting was mailed or such public disclosure made, whichever occurs first. Both the Arizona Bylaws and the Delaware Bylaws further provide that, in the year the advance provisions come into effect, if they come into effect less than one hundred (100) days prior to the anniversary date of the immediately preceding annual meeting of shareholders, notice also would be timely if received by the tenth (10th) day following the day on which the advance notice provisions became effective.

These notice requirements help ensure that shareholders are aware of all proposals to be voted on at the meeting and have the opportunity to consider each proposal in advance of the meeting.

In addition to the relevant bylaw provisions, federal securities laws generally provide that shareholder proposals that the proponent wishes to include in the Company s proxy materials must be received not less than 120 days in advance of the date of the proxy statement released in connection with the previous year s annual meeting.

Anti-takeover Measures. Delaware Law has been widely viewed to permit a corporation greater flexibility in governing its internal affairs and its relationships with stockholders and

other parties than do the laws of many other states. In particular, Delaware Law permits a corporation to adopt a number of measures designed to reduce a corporation s vulnerability to hostile takeover attempts. Among these measures is the establishment of a stockholder rights plan. While certain types of stockholder rights plans have been upheld by Delaware courts, Arizona courts have yet to decide on the validity of many of such defenses, thus rendering their effectiveness in Arizona less certain. As discussed herein, differences between Arizona and Delaware Law, effective without additional action by the Delaware Company, could have a bearing on unapproved takeover attempts.

As further discussed, some of the anti-takeover provisions of Arizona Law may continue to apply to the Company so long as it is deemed an issuing public corporation under Arizona Law. An issuing public corporation is defined as a public company which is either incorporated in Arizona or has its principal place of business or principal executive office in Arizona and owns or controls assets located within Arizona with a fair market value of at least $1 million and has more than 500 employees residing in Arizona.

Delaware Business Combination Law. Section 203 of the Delaware Law (***Section 203***) was adopted by Delaware s legislature to encourage potential acquirors to negotiate with a target company s Board and, in the absence of successful (or any) negotiations, to provide minority stockholders with protections against certain takeover-related abuses.

Section 203 regulates certain transactions incident to or following large accumulations of shares, including those made by tender offers. Section 203 may have the effect of significantly delaying a purchaser s ability to acquire the entire interest sought if such acquisition is not approved by a corporation s Board. In general, Section 203 prevents an Interested Stockholder (defined generally as a person with 15% or more of a corporation s outstanding voting stock), from engaging in a Business Combination, as defined below, with a Delaware corporation for three years following the date such person became an Interested Stockholder. For purposes of Section 203, the term Business Combination includes, without limitation: (a) mergers with the Interested Stockholder; (b) sales or other dispositions to the Interested Stockholder (except proportionately with the corporation s other stockholders) of assets of the corporation or a subsidiary having a market value equal to 10% or more of the aggregate market value of the corporation s consolidated assets or its outstanding stock; (c) the issuance or transfer by the corporation or a subsidiary of stock of the corporation or such subsidiary to the Interested Stockholder (except for certain transfers in a conversion or exchange or a pro rata distribution or certain other transactions, none of which increase the Interested Stockholder s proportionate ownership of any class or series of the corporation s or such subsidiary s stock); (d) any transaction involving the corporation or a subsidiary that increases the proportionate share of the stock or convertible security of the corporation or such subsidiary owned by the Interested Stockholder (except as a result of immaterial adjustments or any purchase or redemption of stock not caused by the Interested Stockholder) or (e) receipt by the Interested Stockholder (except proportionately as a stockholder), directly or indirectly, of any loans, advances, guarantees, pledges or other financial benefits provided by or through the corporation or a subsidiary.

The three-year moratorium imposed on Business Combinations with Interested Stockholders by Section 203 does not apply if, among other things: (a) prior to the date on which such stockholder becomes an Interested Stockholder the Board approves either the Business

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Combination or the transaction that resulted in the person becoming an Interested Stockholder; (b) the Interested Stockholder owns 85% of the corporation s voting stock upon consummation of the transaction that made him or her an Interested Stockholder (excluding from the 85% calculation shares owned by directors who are also officers of the target corporation and shares held by employee stock plans that do not permit employees to decide confidentially (e.g., by giving confidential instructions to a plan s trustee) whether to accept a tender or exchange offer); or (c) on or after the date such person becomes an Interested Stockholder, the Board approves the Business Combination and it is also approved at a stockholder meeting by holders of two-thirds (66 2/3%) of the voting stock not owned by the Interested Stockholder.

Under Section 203, the restrictions described above do not apply if, among other things, the corporation s original certificate of incorporation contains a provision expressly electing not to be governed by Section 203. The Delaware Certificate does not opt out of the statute.

Arizona Business Combinations Law. Arizona law contains a provision (the ***Business Combinations Provision***) that provides, subject to certain exceptions specified therein, that an issuing public corporation may not engage in any business combination (as defined) or vote, consent or otherwise act to authorize a subsidiary of the issuing public corporation to engage in any business combination with respect to, proposed by or on behalf of or pursuant to any agreement, arrangement or understanding with any interested shareholder (as defined below) of the issuing public corporation or any affiliate or associate of the interested shareholder for a three-year period following the date that such shareholder becomes an interested shareholder unless prior to such date (the ***Shares Acquisition Date***) a committee of the Board, formed in the manner described below (the ***Business Combinations Committee***), approved either the business combination or the transaction which resulted in the shareholder becoming an interested shareholder.

After such three-year period, the issuing public corporation may engage in such transactions only if (i) prior to the Shares Acquisition Date, the Board of the issuing public corporation approved either the business combination or the transaction which resulted in the shareholder becoming an interested shareholder; (ii) the business combination is approved by the affirmative vote of the shareholders holding a majority of the voting power of all shares, excluding shares beneficially owned by the interested shareholder or any affiliate or associate of the interested shareholder; or (iii) the business combination meets certain conditions relating to price and form of consideration.

The Business Combinations Provision provides that the Business Combinations Committee shall be comprised of all of the disinterested directors (as defined below) of the issuing public corporation, except that if there are no disinterested directors the Board must select three or more disinterested persons to be committee members. For purposes of the Business Combinations Provision, an interested shareholder is defined to include (i) any person that is the owner of 10% or more of voting power of the outstanding shares of the issuing public corporation or (ii) any affiliate or associate of the issuing public corporation that at any time within the three-year period immediately before the date in question was the beneficial owner of 10% or more of the voting power of the then outstanding shares of the issuing public corporation. For purposes of the Business Combinations Provision, a director or person is deemed to be disinterested if the director or person is not an interested shareholder, an affiliate or associate of an interested

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shareholder or a present or former officer or employee of the issuing public corporation or of an affiliate or associate of the issuing public corporation or of the interested shareholder. An issuing public corporation may amend its articles of incorporation or bylaws, with the approval of shareholders holding a majority of the outstanding voting power of all shares, excluding shares beneficially owned by an interested shareholder whose Share Acquisition Date is prior to the effective date of such amendment from the restrictions imposed under the Business Combinations Provision.

Compensation Agreements. Arizona law provides that during any tender offer or request or invitation for tenders of any class or series of shares of an issuing public corporation, other than an offer by the issuing corporation, the issuing public corporation may not enter into or amend agreements containing provisions that increase the current or future compensation of any officer or director of the issuing public corporation, other than routine increases in compensation or other routine compensation agreements undertaken in the ordinary course of the issuing public corporation s business. Delaware law does not contain a similar provision.

Control Share Acquisitions. Arizona law contains a provision (the ***Control Share Acquisitions Provision***) that generally provides that if any person or group of persons (a ***Purchasing Person***) acquires shares of an issuing public corporation that, when added to all other shares of the issuing public corporation beneficially owned by the Purchasing Person, would result in the percentage of the corporation s voting power that the Purchasing Person is entitled to exercise, or direct the exercise, being increased above certain specified levels (one-fifth, one-third or a majority) of the shares of the corporation, then the Purchasing Person will not have the right to vote the shares in excess of that level, except for the election of directors (the ***Excess Shares***) unless such voting rights are approved by the holders of a majority of the voting power of all shares, excluding all shares beneficially owned by the Purchasing Person or its affiliates or associates or by any officer or director of the issuing public corporation. In addition, unless otherwise provided in the articles of incorporation or in bylaws approved by the shareholders, the issuing public corporation may call for redemption of all but not less than all of the Excess Shares at a redemption price equal to the market value of the shares at the time the call of redemption is given if either (i) the Purchasing Person fails to deliver certain written information to the issuing public corporation by the tenth day after crossing the specified level; or (ii) the shareholders vote not to accord voting rights to such shares. The Purchasing Person must submit for the approvals described above each time such shareholders seek to acquire the power to vote shares at the next level. Delaware law does not contain a provision similar to the Control Share Acquisition Provision.

Duties of Directors. Arizona Law provides that, in discharging the duties of the position of director with respect to corporate takeovers, a director of an issuing public corporation must consider the long-term as well as the short-term interests of the corporation and its shareholders including the possibility that these interests may be best served by the continued independence of the corporation. Delaware law does not contain such a provision.

Limitation of Share Repurchase. Under Arizona Law, an issuing public corporation may not purchase or agree to purchase any shares from a beneficial owner of more than 5% of the voting power of the issuing public corporation for more than the average market price (as defined) of the shares if the shares have been beneficially owned by the beneficial owner for less than three

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years unless either (i) the purchase or agreement to purchase is approved at a meeting of shareholders by the affirmative vote of a majority in interest of the outstanding shares excluding shares beneficially owned by the beneficial owner, its affiliates or associates or by any officer or director of the issuing public corporation; or (ii) the issuing public corporation makes an offer, of at least equal value per share, to all holders of shares of such class or series and to all holders of any class or series into which the shares may by converted. Delaware law does not contain a similar provision.

There can be no assurance that the Board would not adopt any further anti-takeover measures available under Delaware Law (some of which may not require stockholder approval). The availability of anti-takeover measures under Delaware Law, whether or not implemented, may have the effect of discouraging a future takeover attempt which a majority of the Delaware Company s stockholders may deem to be in their best interests or in which shareholders may receive a premium for their shares over then current market prices. As a result, stockholders who might desire to participate in such transactions may not have the opportunity to do so. Stockholders should recognize that, if adopted, the effect of such measures, along with the possibility of discouraging takeover attempts, may be to limit in certain respects the rights of stockholders of the Delaware Company compared with the rights of shareholders of the Company.

Amendment of Bylaws. The Arizona Bylaws and Delaware Bylaws may be repealed, altered or amended, and new bylaws may be enacted by the Board or by the holders of a majority in interest of the outstanding stock of the Company.

Inspection of Shareholder Lists. Arizona Law provides that any shareholder of at least six months or the holder of a beneficial interest of 5% or more of the outstanding stock has a right to inspect the Company records, including shareholder lists. Arizona law also provides that any shareholder has a right to inspect the Company s shareholder list in anticipation of a noticed shareholder meeting.

Delaware Law permits any stockholder of record to inspect the stockholder list for any purpose reasonably related to that person s interest as a stockholder and, under certain circumstances, to inspect the books and records of the corporation.

Appraisal Rights. Arizona Law grants to shareholders the right to dissent in the case of (i) consummation of a plan of merger if the shareholder is entitled to vote on the merger or the corporation is a subsidiary that is merged with its parent, (ii) consummation of a plan of share exchange to which the corporation is a party as the corporation whose shares will be acquired, if the shareholder is entitled to vote on the plan, (iii) a sale or exchange by a corporation of all or substantially all of its property not made in the usual and regular course of its business, if the shareholder is entitled to vote on the sale or exchange, including a sale in dissolution, but not including a sale pursuant to an order of a court or a sale for cash on terms requiring that all or substantially all of the net proceeds of the sale be distributed to the shareholders in accordance with their respective interest within one year after the date of sale, (iv) an amendment of the articles of incorporation that materially adversely affects rights in respect of a dissenter s shares, and (v) any corporate action taken pursuant to a shareholder vote to the extent the articles of incorporation, bylaws or a resolution

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of the Board provides for dissenter s rights. The dissenters right do not apply, unless the corporation s articles of incorporation provide otherwise, to the holders of shares if the shares are listed on a national securities exchange or the Nasdaq National Market or held of record by at least 2,000 shareholders do not have the right to dissent from such corporation action.

Delaware Law grants appraisal rights only in the case of a merger or consolidation and not in the case of a sale or exchange of assets, regardless of the number of shares of stock being issued. Such appraisal rights are not available: (a) with respect to the sale, lease or exchange of all or substantially all of the assets of a corporation; (b) with respect to a merger or consolidation by a corporation the shares of which are either (i) listed on a national securities exchange or designated as a national market system security on an interdealer quotation system by the National Association of Securities Dealers, Inc. or (ii) held of record by more than 2,000 holders if such stockholders receive only shares of the surviving corporation or shares of any other corporation that are either listed on a national securities exchange or designated as a national market system security on an interdealer quotation system by the National Association of Securities Dealers, Inc. or held of record by more than 2,000 holders, plus cash in lieu of fractional shares of such corporations; or (c) to stockholders of a corporation surviving a merger if no vote of the stockholders of the surviving corporation is required to approve the merger under Delaware law.

Delaware Law does not provide stockholders with voting or appraisal rights when a corporation acquires another business through the issuance of its stock in exchange for assets or stock or in a merger with a subsidiary.

Because the Company s Common Stock is currently listed on the Nasdaq National Market, appraisal rights will not be available under Arizona Law to the Company s shareholders in connection with the reincorporation in Delaware.

Dividends and Redemptions. Under Arizona Law, the directors of every corporation are permitted, subject to the articles of incorporation, to make distributions to shareholders unless, after giving effect to such a distribution, the corporation would not be able to pay its debts as they become due in the usual course of business, or the corporation s total assets would be less than the sum of its total liabilities plus the amount that would be needed to satisfy the dissolution rights of shareholders whose preferential rights are superior to those receiving the distribution.

Delaware Law allows the payment of dividends out of surplus (including paid-in and earned surplus) or, in certain circumstances, out of net profits for the current and immediately preceding fiscal years. Shares may be redeemed or repurchased out of surplus, or, in limited circumstances, out of capital. The Company expects that its ability to pay cash dividends in accordance with its prior practices will not be affected by the Reincorporation.

Dissolution. Under Arizona Law, the Board is required to recommend dissolution to the shareholders and the shareholders entitled to vote shall approve the proposal by a majority in interest of the outstanding shares unless the articles of incorporation requires a greater vote. The Arizona Articles do not require a greater vote.

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Under Delaware Law, dissolution requires either the approval of the Board and a majority of the outstanding shares, or unanimous approval of the stockholders.

Interests of the Company s Directors and Officers

The Company s shareholders should be aware that reincorporation in Delaware may be of benefit to the Company s directors by reducing the directors potential personal liability and increasing the scope of permitted indemnification, by strengthening the directors ability to resist a takeover bid, and in other respects. The Reincorporation is not intended to and will not affect the rights of any parties to any of the lawsuits to which the Company is a party. The interests of the Board in recommending the Reincorporation may therefore be in conflict with the interests of the shareholders, and the interests of the Board, management and affiliated shareholders in voting on the Reincorporation proposal may not be the same as those of unaffiliated shareholders.

Federal Income Tax Consequences of the Reincorporation

The following discussion addresses the material federal income tax considerations that are generally applicable to holders of Common Stock of the Company who receive Common Stock of the Delaware Company in exchange for their Common Stock of the Company in the Reincorporation. This discussion does not address all of the tax consequences of the Reincorporation that may be relevant to particular of the Company s shareholders in light of their particular circumstances, such as shareholders who are dealers in securities, who are foreign persons, who do not hold their Common Stock of the Company as Capital Assets or who acquired their Common Stock of the Company through stock option or stock purchase programs or in other compensatory transactions. The tax consequences to holders of options to acquire Common Stock of the Company are also not discussed herein. In addition, the following discussion does not address the tax consequences of transactions effected prior to or after the Reincorporation (whether or not such transactions are in connection with the Reincorporation). Finally, no foreign, state or local tax considerations are addressed herein. Accordingly, the Company s shareholders are urged to consult their own tax advisors as to the specific tax consequences to them of the Reincorporation and related transactions, including the applicable federal, state, local and foreign tax consequences to them of the Reincorporation and such related transactions.

The following discussion is based on the interpretation of the Internal Revenue Code of 1986, as amended (the ***Code***), applicable Treasury Regulations, judicial authority and administrative rulings and practice, all as of the date hereof. The Internal Revenue Service (the ***IRS***) is not precluded from adopting a contrary position. In addition, there can be no assurance that future legislative, judicial or administrative changes or interpretations will not adversely affect the accuracy of the statements and conclusions set forth herein. Any such changes or interpretations could be applied retroactively and could affect the tax consequences of the Reincorporation to the Company, the Delaware Company and/or the Company s shareholders. A ruling from the Internal Revenue Service will not be requested in connection with the Reincorporation.

Subject to the limitations, qualifications and exceptions described herein, and assuming the Reincorporation qualifies as a reorganization within the meaning of Section 368(a) of the Code (a ***Reorganization***), the following federal income tax consequences will generally result:

No gain or loss will be recognized by holders of the Common Stock of the Company upon receipt of Common Stock of the Delaware Company pursuant to the Reincorporation;

The aggregate tax basis of the Common Stock of the Delaware Company received by each shareholder of the Company in the Reincorporation will be equal to the aggregate tax basis of the Common Stock of the Company surrendered in exchange therefor;

The holding period of the Common Stock of Delaware Company received by each shareholder of the Company will include the period for which such shareholder held the Common Stock of the Company surrendered in exchange therefor, provided that such Common Stock of the Company was held by such shareholder as a capital asset at the time of the Reincorporation; and

No gain or loss will be recognized by the Company or Delaware Company as a result of the Reincorporation.

Although a successful IRS challenge to the Reorganization status of the Reincorporation is unlikely, such a challenge should result in a shareholder recognizing gain or loss with respect to each share of Common Stock of the Company exchanged in the Reincorporation equal to the difference between the shareholder s basis in such share and the fair market value, as of the time of the Reincorporation, of the Common Stock of the Delaware Company received in exchange therefor. In such event, a shareholder s aggregate basis in the shares of Common Stock of the Delaware Company received in the exchange would equal the fair market value of such shares at the time of the Reincorporation, and the shareholder s holding period for such shares would begin the day after the Reincorporation.

The Company s shareholders will be required to attach a statement to their tax returns for the year of the Reincorporation that contains the information listed in Treasury Regulation Section 1.368-3(b). Such statement must include, among other things, the shareholder s tax basis in the shareholder s Common Stock of the Company and a description of the Common Stock of the Delaware Company received.

Other Regulatory Requirements

Except as set forth above, no federal or state regulatory requirements must be complied with nor must approvals be obtained in connection with the Reincorporation, except under federal securities laws applicable to proxy solicitations.

Rule 144

Under Rule 144 under the Securities Act of 1933, as amended, the holding period for the Delaware Company Common Stock received in exchange for Company Common Stock will include the period during which Company Common Stock was held.

Required Approvals

The affirmative vote of holders of a majority of the outstanding shares of Company Common Stock, is required for approval of the Reincorporation.

Mr. Mihaylo s Recommendation in Opposition

Mr. Mihaylo asserts that there is no need for the Company to go through the expense or resulting distraction of management s attention associated with reincorporation in Delaware. As more fully described above, the Reincorporation and resulting conversion to Delaware law is largely an administrative process. In fact, migrating to Delaware law will actually allow the board to operate more efficiently as the majority of the directors of the corporation are more familiar with Delaware law, and Delaware law is clear on many matters either not addressed, or with respect to which there is little precedent, under Arizona law. Most public corporations in the United States are incorporated in Delaware.

Mr. Mihaylo suggests that the Company s assertion, that reincorporation under Delaware law will enhance the Company s ability to attract and retain qualified officers and directors, is inconsistent with the Company s claim that it has not experienced difficulty in retaining officers to date. While it is true that the Company has not had trouble to date attracting qualified officers and directors, the current climate with respect to corporate governance leads the Company to believe that it may be more difficult in the future to retain good management. In the wake of the implementation of the Sarbanes-Oxley Act of 2002 and the litigation relating to the corporate governance failures that inspired it, quality candidates are increasingly hesitant to join boards due to personal liability concerns. This is particularly so when a corporation is in a high-profile phase and may likely have to make major strategic decisions, as is the case currently with the Company. Delaware has the most definitive law on matters of director indemnification, and the clarity and predictability of Delaware law are important for recruiting and retaining quality directors. Contrary to Mr. Mihaylo s assertion that the director indemnification seems to more directly benefit the members of the Inter-Tel Board than the Inter-Tel shareholders, the Board believes that the Reincorporation and resulting clarity and predictability associated with being a Delaware corporation is mutually beneficial to the Inter-Tel Board and to all of the Inter-Tel shareholders.

Finally, we consider Mr. Mihaylo s concern regarding distracting management s attention from the running of the business (page 14) somewhat disingenuous, as his actions of late seem intended to cause far greater distraction to management than would result from the administrative process of the Reincorporation.

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THE BOARD OF DIRECTORS RECOMMENDS THE SHAREHOLDERS VOTE FOR PROPOSAL NO. 2.

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TO APPROVE A SPECIAL RESOLUTION AUTHORIZING THE COMPANY S BOARD OF DIRECTORS TO EFFECT AN AMENDMENT TO THE COMPANY S CHARTER DOCUMENTS REQUIRING THE APPROVAL OF A MAJORITY OF DISINTERESTED SHAREHOLDERS TO EFFECT CERTAIN BUSINESS COMBINATION TRANSACTIONS INVOLVING INTERESTED PARTIES

(Proposal No. 3)

The Board recommends that the shareholders approve a special resolution authorizing the Board to amend the Arizona Articles, or, in the event that Proposal No. 2 is approved, include in the Delaware Certificate a provision, to require the approval of a majority of the disinterested shareholders to effect certain business combination transactions involving shareholders holding 15% or more of the Company s stock (***Interested Shareholders***).

The Board believes that such a provision is in the best interests of the shareholders because it may have the effect of delaying an Interested Shareholder s ability to acquire the corporation and because it would require an Interested Shareholder to seek significant agreement from other shareholders, helping to deflect abusive takeover tactics and helping ensure that shareholders and the Board have the means and opportunity to obtain the best price and the most favorable terms for any proposed takeover of the Company.

The proposed provision has been drafted to mirror in many respects Section 203 of the Delaware Law, as described in detail in Proposal No. 2. The principal differences between the statutory regime and the proposed charter provision are (i) that the charter provision would apply to all Interested Shareholders, regardless of when such an Interested shareholder acquired a 15% interest in the Company s voting stock or for how long such an Interested Shareholder has held such interest and (ii) rather than requiring the approval of two-thirds of the disinterested shareholders to consummate a business transaction as required by Section 203 of the Delaware Law, the proposed provision would require the approval of only a majority of disinterested shareholders. The Board believes that these alterations will provide wider protections against takeover abuses by Interested Shareholders than those afforded by statute without imposing more onerous approval burdens.

Due to the increased burden it places on takeover attempts, the provision may have the effect of discouraging a future attempt to acquire control of the Company that is not presented to and approved by the Board, but that a substantial number of the shareholders might believe to be in their best interests or in which shareholders might receive a substantial premium for their shares over then current market prices. As a result of such effects, shareholders who might desire to participate in such a transaction may not have an opportunity to do so. In addition, unapproved tender offers and takeover attempts may be made at times and in circumstances that are beneficial to and in the interests of certain shareholders. Furthermore, a negotiated transaction is not necessarily more advantageous to the shareholders than a non-negotiated transaction.

Mr. Mihaylo has asserted that there is no need to incorporate the proposed provision into the Company s charter because the Company can simply negotiate such a requirement. Mr. Mihaylo s suggestion disregards the primary purpose of

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Proposal Number 3 which is to guard against hostile bids for control of the Company in respect of which there is no opportunity to negotiate. In the context of a hostile bid there would be no opportunity to negotiate such a requirement, and the proposed provision is helpful to maintain control over process and defend against coercive offers. Even in a negotiated transaction with an insider, an interested party is disinclined to agree to risk submitting the transaction to a vote of the disinterested shareholders of a company. In such circumstances the board of directors of a corporation will likely establish a special committee of disinterested board members to negotiate the terms of the transaction on an arm s length basis.

The Company believes that absent the adoption of Proposal Number 3, Mr. Mihaylo, by virtue of his current holdings in the Company and his access during his tenure as CEO to information not generally available to Company shareholders, could place the other shareholders of the Company at a considerable disadvantage. If Mr. Mihaylo were to follow through on his publicly-stated intention to make an offer for the Company, his current holdings could allow him to force a transaction, even if such a transaction is disfavored by the majority of the disinterested shareholders and by the Board. The Company believes that under these circumstances, approval of such a transaction should require a majority of the disinterested shareholders, and Proposal Number 3 ensures this process.

If this Proposal No. 3 is approved, the Board will be authorized to include in the Arizona Articles (or the Delaware Certificate if Proposal No. 2 related to the Reincorporation is approved) a proposal substantially as set forth on Annex D, as adjusted for the Arizona Articles or the Delaware Certificate, as applicable.

THE BOARD OF DIRECTORS RECOMMENDS THE SHAREHOLDERS VOTE FOR PROPOSAL NO. 3.

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RATIFICATION OF APPOINTMENT OF INDEPENDENT AUDITORS

(Proposal No. 4)

The Audit Committee of the Board of Directors has appointed Ernst & Young LLP as independent auditors to audit the consolidated financial statements of the Company and its subsidiaries for the year ending December 31, 2006. Although Inter-Tel is not required to seek shareholder ratification of this appointment, the Board of Directors believes it to be sound corporate governance to do so. If the appointment is not ratified, the Audit Committee will investigate the reasons for shareholder rejection and will reconsider the appointment.

Ernst & Young LLP has issued its report, included in the Company s Form 10-K, on the consolidated financial statements of the Company for the year ending December 31, 2005. Ernst & Young LLP has served as the Company s independent auditors in every year in which the Company s stock has been publicly traded.

Before selecting Ernst & Young LLP, the Audit Committee carefully considered Ernst & Young LLP s qualifications as independent auditors. This included a review of the qualifications of the engagement team, the quality control procedures the firm has established, any issues raised by the most recent quality control review of the firm, as well as its reputation for integrity and competence in the fields of accounting and auditing.

Fees Billed by Ernst & Young LLP During Fiscal 2005 and 2004.

The Audit Committee has established a policy of pre-approving audit and non-audit services provided by the auditors of Inter-Tel. Each of the fees for services listed below for 2005 were pre-approved by Inter-Tel s Audit Committee. The Audit Committee s review included matters to be considered under the rules of the SEC, including the nature and extent of non-audit services, to ensure that the auditors independence would not be impaired. The Audit Committee expressed its satisfaction with Ernst & Young LLP in all of these respects. The Audit Committee of our board of directors has determined that the provision of services by Ernst & Young LLP other than for audit related services is compatible with maintaining the independence of Ernst & Young LLP as our independent auditors.

The following table sets forth the approximate aggregate fees billed by Ernst & Young LLP to Inter-Tel during fiscal 2005 and 2004:

	2005	2004
Audit Fees (1) Audit of consolidated financial statements	$ 283,000	$ 231,000
Sarbanes-Oxley section 404 attestation of internal controls	431,000	439,000
Statutory audit of Lake Communications	42,000	
Timely quarterly reviews	62,000	55,500
Total Audit Fees	818,000	725,500
Audit-Related Fees (2)		

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	2005	2004
Consultation on SEC matters		2,200
Section 404 assistance		5,500
Total Audit-Related Fees		7,700
All Other Fees (2) Form S-8, Stock Options and Other	2,500	2,500
Total All Other Fees	2,500	2,500
Total Fees	$ 820,500	$ 710,700

(1) Includes fees and expenses related to the fiscal year audit and interim reviews, notwithstanding when the fees and expenses were billed or when the services rendered.

(2) Includes fees and expenses for services rendered from January through December of the fiscal year, notwithstanding when the fees and expenses were billed.

The Company did not engage Ernst & Young LLP to provide any separate information technology services during the fiscal years ended December 31, 2005 or 2004. Representatives of Ernst & Young LLP are expected to be present at the Annual Meeting and will have the opportunity to make a statement if they desire to do so, and will be available to respond to appropriate questions.

The affirmative vote of a majority of the votes cast on this proposal shall constitute ratification of the appointment of Ernst & Young LLP.

THE BOARD UNANIMOUSLY RECOMMENDS THAT THE SHAREHOLDERS VOTE FOR THE RATIFICATION OF THE APPOINTMENT OF ERNST & YOUNG LLP AS THE COMPANY S INDEPENDENT AUDITORS FOR FISCAL YEAR 2006.

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TO ADJOURN THE ANNUAL MEETING, IF NEEDED, TO SOLICIT ADDITIONAL VOTES
(Proposal No. 5)

At the Annual Meeting, if the Board of Directors determines that the Company needs additional time to solicit votes to approve any or all of Proposals 1 through 4, the shareholders are being asked to vote upon a proposal to adjourn the annual meeting for the purpose of allowing additional time for the solicitation of additional votes. The Company presently intends to exercise such authority at the Annual Meeting if the majority of the Board of Directors present at the Annual Meeting determines that such adjournment may increase the likelihood of obtaining sufficient votes to approve any or all of Proposals 1 through 4.

THE BOARD OR DIRECTORS RECOMMENDS THAT SHAREHOLDERS VOTE IN FAVOR OF THE PROPOSAL TO ADJOURN THE MEETING, IF NECESSARY TO PROVIDE MORE TIME TO SOLICIT ADDITIONAL VOTES FOR PROPOSALS 1 THROUGH 4.

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THE SELL THE COMPANY RESOLUTION
(Proposal No. 6)

RESOLVED, that the shareholders of Inter-Tel Incorporated (Inter-Tel) urge the Inter-Tel Board of Directors to arrange for the prompt sale of Inter-Tel to the highest bidder.

Supporting Statement

The reason for the Sell the Company Resolution is to give all the shareholders the opportunity to send a message to the Inter-Tel Board that the shareholders support the sale of Inter-Tel to the highest bidder. Even if approved by the shareholders at the Meeting, the Sell the Company Resolution will not be binding on the Inter-Tel Board. Mr. Mihaylo believes, however, that if the Sell the Company Resolution receives substantial support from shareholders, the Inter-Tel Board may choose to carry out the request set forth in the Sell the Company Resolution.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ADOPTION OF THE SELL THE COMPANY RESOLUTION.

The Board of Directors is committed to maintaining the highest standards of corporate governance and fully understands its duty to act in the best interest of the Shareholders in managing and supervising the affairs of the Company. The Board is independent; only one of the eight directors on the Board is an employee of the Company. A majority of the members of the Board are also shareholders in the Company.

The Board regularly evaluates the Company s long-term strategic objectives and among its key objectives is the enhancement of shareholder value. In pursuit of this objective, the Board has engaged UBS Investment Bank and other experts to help build and grow the Company and achieve its long-term strategic objectives. The Board is not opposed to exploring the sale of the Company as a means to maximize shareholder value, if in good faith the Board were able to reasonably determine that such a sale would result in a better long-term return to shareholders as opposed to continuing to pursue the Company s strategic business plan.

The Board opposes the proposed resolution as it would forestall members of the Board from considering alternatives other than a sale of the Company as a means to enhance shareholder value. If the Board was to pursue a sale of the Company to the exclusion of other potential strategic alternatives, it would result in a disregard of the Board s fiduciary duties to select the best alternative for the enhancement of shareholder value. Further, such a strategy could create a forced sale atmosphere, in which the Company would be forced to negotiate with potential bidders from a position of weakness, possibly resulting in a reduction of the perceived value of the Company. The Board believes that a sale process contemplating an unspecified transaction could be harmful to the Company s day-to-day operations and would create unnecessary uncertainty among the Company s lenders, employees, vendors, customers and other stakeholders, to the resulting detriment of the Company s shareholders. Finally, our Board is confident in the

management of the Company under the leadership of the Company s new Chief Executive Officer, Norman Stout, and in the introduction of the Company s Inter-Tel 5600 communications system and the Company s latest next generation communications platform, the Inter-Tel 7000, which is scheduled for release this year.

As the Inter-Tel 5600 and the Inter-Tel 7000 platforms were conceived during Mr. Mihaylo s tenure as Chief Executive Officer, he possesses an understanding of the potential long-term potential benefits to shareholders associated with the new platforms implementation. While Mr. Mihaylo has recently expressed publicly his concern as to the ability of the Company to successfully transition to its new products, he has also publicly stated his intention to make an offer to purchase the Company. By publicly expressing such a concern, Mr. Mihaylo could undermine shareholder confidence in the Company s long-term prospects and take advantage of such reduced confidence by buying the Company at less than full value.

Selling the Company now to third parties may prevent Company shareholders from realizing potential value from the Company s substantial investment in its new platform as potential buyers may discount such benefits due to the uncertainty of the platform s success. In the opinion of the Board the Company will be best able to enhance shareholder value by focusing on the Company s continued success under its current management, but consistent with its fiduciary duties will carefully consider any bona fide third party offer which the Board believes has the potential to increase shareholder value.

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THE REPEAL THE BYLAW AMENDMENT RESOLUTIONS
(Proposal No. 7, 8 and 9)

RESOLVED, that the amendments to Section 2.5 (Special Meetings of Shareholders) of the Bylaws of Inter-Tel, Incorporated adopted by the Board of Directors on February 21, 2006, relating to the calling of a special meeting of shareholders for the purpose of considering any action to directly or indirectly facilitate a business combination are hereby repealed.

RESOLVED, that Section 2.12 (Advance Notice of Shareholder Business) of the Bylaws of Inter-Tel, Incorporated adopted by the Board of Directors on March 29, 2006 is hereby repealed in its entirety.

RESOLVED, that Section 2.13 (Advance Notice of Director s Nominations) of the Bylaws of Inter-Tel Incorporated adopted by the Board of Directors on March 29, 2006 is hereby repealed in its entirety.

Supporting Statement

The reason for the Repeal the Bylaw Amendments Resolutions is to give all shareholders the opportunity to repeal the amendments to Section 2.5 and to repeal in their entireties Sections 2.12 and 2.13 of the Inter-Tel Bylaws recently adopted by the Inter-Tel Board. Prior to the recent amendments a 10% Shareholder could call a special meeting of Shareholders, even with respect to a business combination transact, and no advance notice was required under the Inter-Tel Bylaws for Shareholder nominations for the election of directors or conduct of business at the General Meeting of Shareholders. Recent amendments to Section 2.5 and the adoption of Sections 2.12 and 2.13 of the Bylaws could have the effect of discouraging offers to acquire Inter-Tel. Together with the Sell the Company Resolution, Mr. Mihaylo believes that the Repeal the Bylaw Amendments Resolutions would send a strong message to the Inter-Tel Board that the shareholders support the sale of Inter-Tel to the highest bidder and that the Board of Directors should not adopt amendments to the Bylaws that could discourage offers to acquire Inter-Tel.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ADOPTION OF THE REPEAL THE BYLAW AMENDMENTS RESOLUTIONS.

On February 21, 2006 and March 29, 2006, the Board of Directors of the Company, in consultation with its professional advisors, adopted amendments to the Amended and Restated Bylaws of the Company which, among other items, modified the Company s existing Bylaws to (i) revise provisions relating to the ability of the shareholders of the Company to call a special meeting of the shareholders for the purposes of facilitating a business combination transaction or affecting the composition of the Board for that purpose, (ii) require shareholders bringing business before an annual meeting of the Company s shareholders to provide the Company with advance notice of such business and (iii) require shareholders nominating directors for election at an annual meeting of the Company s shareholders to provide the Company with advance notice of such nominations. The provisions are included in the Company s Amended and Restated Bylaws as

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Sections 2.5, 2.12 and 2.13, respectively and are hereinafter referred to as the Bylaw Amendments.

Section 2.5 was amended to add an exception to the ability of shareholders owning at least ten percent (10%) of the Company s issued and outstanding capital stock may call a special meeting of shareholders. The exception is that a special meeting for the purpose of considering any action to directly or indirectly facilitate a business combination transaction, including any action to change or otherwise affect the Board for that purpose, may only be called at the request in writing of shareholders owning at least twenty-five percent (25%) of the Company s issued and outstanding capital stock. This exception is expressly provided for under Arizona Corporation Law Section 10-2703 which states that Special meetings of the shareholders...may be called for any purpose or purposes...at any time by...a shareholder or shareholders holding ten per cent or more of the voting power of all shares, except that a special meeting for the purpose of considering any action to directly or indirectly facilitate or effect a business combination, including any action to change or otherwise affect the composition of the board of directors for that purpose, must be called by twenty-five per cent or more of the voting power of all shares.

Section 2.12 is a new provision that provides that, in order to be properly brought before an annual meeting, any business must be (i) specified in the notice of meeting given by the Company, (ii) otherwise properly brought before the meeting by or at the direction of the Board, or (c) otherwise properly brought before the meeting by a shareholder as set forth in the Bylaws. In order for a shareholder to timely bring business before such an annual meeting, such shareholder must provide notice to the Company not less than ninety (90) days prior to the anniversary date of the immediately preceding annual meeting or, if an annual meeting is called for a date not within thirty (30) days before or after such anniversary date, not later than the tenth (10th) day following the day on which such notice of the date of the meeting was announced. New Section 2.12 also provides that in the event it becomes effective less than one hundred (100) days prior to the anniversary date of the immediately preceding annual meeting of shareholders, notice by the shareholder would also be timely if received not later than the close of business on the tenth (10th) day following the day on which new Section 2.12 became effective. Section 2.12 also prescribes the proper form and content of such a notice, among other things.

Section 2.13 is a new provision that provides that, in order for director nominations to be properly made for and voted upon at an annual meeting of Company shareholders, such nominations must be (i) specified in the notice of meeting given by the Company, (ii) made by or at the direction of the Board, or (c) otherwise properly brought before the meeting by a shareholder as set forth in the Bylaws. In order for a shareholder to timely make nominations of directors to be voted upon at an annual meeting of the Company s shareholders, such shareholder must provide notice of such nominations to the Company not less than ninety (90) days prior to the anniversary date of the immediately preceding annual meeting or, if an annual meeting is called for a date not within thirty (30) days before or after such anniversary date, not later than the tenth (10th) day following the day on which such notice of the date of the meeting was announced. New Section 2.13 also provides that in the event it becomes effective less than one hundred (100) days prior to the anniversary date of the immediately preceding annual meeting of shareholders, notice by the shareholder would also be timely if received not later than the close of business on the tenth (10th) day following the day on which new Section 2.13 became effective. Section 2.13 also prescribes the proper form and content of such a notice, among other things and specifies that such a notice shall in each case include a written consent of the nominee to such nomination.

Mr. Mihaylo was a member of the Board of Directors at the time the Board approved the Section 2.5 Bylaw Amendment, determining at such time that the amendment was in the best interest of the Company.

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The increased share ownership percentage required by Section 2.5 ensures that only potential third party acquirors with a significant stake in the Company have the ability to call a special meeting of the Company for the purpose of a business combination. It conforms the Company s Bylaw provision to Arizona law. The advance notice procedure provided in Section 2.12 provides the Board with an opportunity to inform shareholders of any business proposed to be conducted at a meeting and the Board s position on any such proposal, enabling shareholders to better determine whether they desire to attend the meeting or grant a proxy to the Board as to the disposition of such business. In addition, the business procedure allows for a more orderly procedure for conducting the annual meeting of shareholders. By requiring advance notice of nominations by shareholders, the nomination procedure provided in Section 2.13 affords the Board an opportunity to consider the qualification of the proposed nominees and, to the extent deemed necessary or desirable by the Board of Directors, to inform the shareholders about such qualifications.

The Bylaw Amendments could discourage a third party from conducting a solicitation of proxies to elect its own slate of directors or otherwise attempting to gain control of the Company, even if the conduct of such business or such attempt might be beneficial to the Company, and its shareholders. The existence of anti-takeover provisions (whether the intention of these provisions is to effect an anti-takeover plan or whether the anti-takeover effect is merely incidental) has disadvantages and advantages to shareholders. On the one hand, the existence of anti-takeover provisions may tend to lower the market price of the Company s common stock, as the Company could be considered less attractive to third parties who would otherwise be interested in accumulating stock in a takeover attempt, but are discouraged from doing so because of the anti-takeover provisions. Conversely, the existence of anti-takeover provisions may be beneficial by rendering the Company less vulnerable to a takeover if the market price of its common stock is considered to be low relative the its perceived value. In such a case management would be relieved from pressure to enter into transactions or take other actions that might not be in the best interest of the shareholders.

In the opinion of the Board, the Section 2.5 Bylaw Amendment merely conformed the Company s bylaws to Arizona law, and the Section 2.12 and 2.13 advance notice Bylaw Amendments are standard provisions found in the Bylaws of similarly situated companies. The benefits of the Bylaw Amendments in facilitating the Board s ability exercise its fiduciary duties on behalf of the shareholders of the Company and providing management enhanced ability to respond to indications of interest from third-parties with a credible negotiating position outweigh any potentially detrimental effects and as such serve to enhance shareholder value.

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THE UNANIMOUS VOTE RESOLUTION
(Proposal No. 10)

RESOLVED, that the Bylaws of Inter-Tel, Incorporated are hereby amended to require the unanimous vote of all members of the Board of Directors in order to adopt any amendment to the Bylaws that could have an anti-takeover effect, including, without limitation, any advance notice requirements for the election of directors or the conduct of business at shareholder meetings or any change in the ability of shareholders to call a special meeting of shareholders.

Supporting Statement

The reason for the Unanimous Vote Resolution is to prevent the Inter-Tel Board from amending the Bylaws after the Annual Meeting to create new obstacles to the sale of Inter-Tel to the highest bidder or overturning the vote of the shareholders on the Repeal the Bylaw Amendments Resolutions without the unanimous vote of all members of the Inter-Tel Board. If any of the director nominees proposed by Mr. Mihaylo are elected at the Annual Meeting, then the Inter-Tel Board may not be able to obtain a unanimous vote on any such amendments, although the result of any such vote would depend upon the exercise of each such director s fiduciary duty at the time of the vote. Based upon the number of shares that Mr. Mihaylo beneficially owns and cumulative voting under Arizona law, Mr. Mihaylo will be able to elect at least one director at the Annual Meeting.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ADOPTION OF THE UNANIMOUS VOTE RESOLUTION.

The proposal requests that the Company adopt a unanimous voting standard for board decisions which would involve any amendment to its governing documents that could have an anti-takeover effect. The Company, like many other similarly situated corporations, currently has in place a limited number of measures designed to protect shareholders and maximize shareholder value in the event of a takeover attempt that it views as not being in the best interests of all shareholders. The requirement of a unanimous vote to approve any amendment to the Bylaws of the Company which could potentially have an anti-takeover effect would undermine the ability of the Board to respond quickly and effectively to hostile takeover attempts. The proposal would result in the inability of the Board to act at any meeting where a single director was absent. Further, the proposal would be detrimental to the Board s ability to function cohesively at such time when the Board s working together effectively is critical. Finally, the proposal would effectively grant a veto right to a proposed transaction to any one member. Accordingly, in the Board s opinion, the proposal could lead to a deadlock of the Board and would not be conducive to the Board s goal of enhancing shareholder value.

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THE NO AMENDMENTS RESOLUTION

(Proposal No. 11)

RESOLVED, that each and every provision of the Bylaws of Inter-Tel, Incorporated adopted by the Board of Directors after March 29, 2006, and prior to the adoption of this resolution is hereby repealed.

Supporting Statement

The reason for proposal 6 (the No Amendments Resolution) is to prevent the Inter-Tel Board from taking actions to amend the Bylaws to attempt to nullify or delay the actions to be taken by the shareholders at the Annual Meeting or to create new obstacles to the sale of Inter-Tel to the highest bidder. According to publicly available information, the most recent amendments to the Bylaws were adopted on March 29, 2006 and no amendments subsequent to that date have been publicly disclosed. If the Inter-Tel Board has adopted any amendments to the Bylaws since March 29, 2006, or adopts any amendments to the Bylaws prior the Annual Meeting, the No Amendments Resolution would repeal all such amendments.

THE BOARD OF DIRECTORS RECOMMENDS A VOTE AGAINST ADOPTION OF THE NO AMENDMENTS RESOLUTION.

The Company s Board believes it has demonstrated strong corporate governance policies and practices and that its leadership has consistently resulted in returning value to its shareholders. As discussed in the statement of opposition to the Repeal the Bylaws Resolution, the Board is confident that the Bylaw Amendments are in the best interests of its shareholders. In order to remain responsive to changing business developments, the Board and the management of the Company must be permitted to exercise their discretion in respect of corporate governance matters. Paramount among the means through which the Board is able to do so is through its ability to update and modify the Bylaws of the Company as it considers in the best interest of shareholders. The proposal would effectively prevent the Board from fulfilling one of its most important roles in the exercise of its fiduciary responsibilities on behalf of its shareholders. Accordingly, the Board recommends that you vote against the No Amendments Resolution.

THE BOARD OF DIRECTORS BELIEVES THAT MR. MIHAYLO S PROPOSED RESOLUTIONS ARE NOT IN THE SHAREHOLDERS BEST INTERESTS AND OPPOSES SUCH RESOLUTIONS.

WE STRONGLY RECOMMEND THAT YOU REJECT MR. MIHAYLO S PROPOSED RESOLUTIONS AND URGE YOU NOT TO SIGN OR RETURN ANY PROXY CARD THAT MR. MIHAYLO MAY SEND YOU. WE URGE YOU TO DISREGARD ANY SUCH PROXY SOLICITATION AND TO SIGN AND DATE THE ENCLOSED WHITE PROXY CARD AND RETURN IT TODAY IN THE POSTAGE PAID ENVELOPE PROVIDED.

CORPORATE GOVERNANCE AND OTHER MATTERS

Board Meetings and Committees

The Board of Directors of the Company held a total of four (4) regularly scheduled meetings during the fiscal year ended December 31, 2005 and six (6) special meetings. The Board of Directors has Audit, Compensation, and Corporate Governance and Nominating Committees. Each of these committees has adopted a written charter. All members of the committees are appointed by the Board of Directors, and are non-employee directors. The Board of Directors also held numerous special board meetings and special committee and special subcommittee meetings during 2005. The information provided below describes each committee, its current membership, the number of meetings held during fiscal year 2005 and its function.

During the fiscal year ended December 31, 2005, each director attended all of the Board meetings with the following exception: Ms. Winkler was unable to attend the board meeting on April 26, 2005 due to a prior commitment. Dr. Roland Haden served as a member of the Board from the beginning of 2005 through his resignation effective November 1, 2005; Dr. Haden attended all of the Board meetings during his tenure in 2005.

Director Independence

The Board of Directors has determined that each of its current directors, including all directors standing for re-election, except the Chief Executive Officer, has no material relationship with Inter-Tel and is independent within the meaning of the NASDAQ Stock Market, Inc. (***Nasdaq***) director independence standards, as currently in effect and as they may be changed from time to time.

Audit Committee

The Audit Committee of the Board of Directors consists of directors Chapman, Anderson, Cappello and Edens and, until July 22, 2005 when he resigned from the Audit Committee, Dr. Roland Haden was also a member of the Audit Committee. Each of the current members of the Committee is independent within the meaning of the Nasdaq director independence standards, as currently in effect, and Dr Haden was independent by such standards during his tenure as well. The Board of Directors has determined that director Chapman is an Audit Committee financial expert as defined in SEC rules. Mr. Chapman serves as Chairman of the Audit Committee.

Pursuant to the Audit Committee Charter, the Audit Committee reviews, acts and reports to the Board of Directors of the Company on various auditing and accounting matters, including the appointment of the Company s independent auditors, the scope of the Company s annual audits, fees to be paid to the Company s independent auditors, the performance of the Company s independent auditors, the sufficiency of the Company s internal controls and the Company s accounting and financial management practices.

The Audit Committee met four (4) times during the last fiscal year. The Audit Committee also meets with our independent auditors in an executive session, without the presence of our management, on a quarterly basis, following completion of their quarterly reviews and annual audit and prior to our earnings announcements, to review the results of their work. The Audit

Committee Charter, as amended, is attached as Exhibit A to this Proxy Statement. A report of the Audit Committee is set forth below.

Compensation Committee

The Compensation Committee currently consists of directors Anderson, Winkler and Rodin. Mr. Rodin joined the committee March 29, 2006. Mr. Edens was a member of the Compensation Committee until July 22, 2005, when Ms. Winkler joined the Committee in his place. Dr. Roland Haden was also a member of the Compensation Committee through the date of his retirement from the board of directors effective November 1, 2005. Each of the members of the Compensation Committee is independent within the meaning of the Nasdaq director independence standards, as currently in effect and as they may be changed from time to time, and Dr. Haden was independent for such purposes during his tenure. The Compensation Committee reviews employee compensation and makes recommendations thereon to the Board of Directors and administers the Company s stock incentive plans. The Compensation Committee also determines, upon review of relevant information, the employees to whom options shall be granted. Mr. Anderson serves as Chairman of the Compensation Committee. The Compensation Committee met three (3) times during the last fiscal year. The Charter of the Compensation Committee was attached as Exhibit A to Inter-Tel s Proxy Statement filed on March 18, 2004. A report of the Compensation Committee is set forth below.

Compensation Committee Interlocks and Insider Participation

During fiscal year 2005, no member of the Compensation Committee was an officer or employee of Inter-Tel. During fiscal year 2005, no member of the Compensation Committee or executive officer of Inter-Tel served as a member of the Board of Directors or Compensation Committee of any entity that has an executive officer serving as a member of our Board of Directors or Compensation Committee.

Corporate Governance and Nominating Committee

The Corporate Governance and Nominating Committee consists of directors Edens, Cappello, Chapman, Karol and Winkler, each of whom is independent within the meaning of the Nasdaq director independence standards, as currently in effect and as they may be changed from time to time. The Corporate Governance and Nominating Committee was formed in February 2004 and met five (5) times during the last fiscal year. Mr. Cappello joined the Committee on December 20, 2005. Dr. Roland Haden was also a member of the Committee through the date of his retirement from the board of directors effective November 1, 2005. Mr. Karol joined the committee March 29, 2006. Mr. Edens serves as Chairman of the Corporate Governance and Nominating Committee. The Charter of the Corporate Governance and Nominating Committee was attached as Exhibit B to Inter-Tel s Proxy Statement filed on March 18, 2004.

The responsibilities of the Corporate Governance and Nominating Committee include:

- considering and periodically reporting on matters relating to the identification, selection and qualification of the Board of Directors and candidates nominated to the Board of Directors and its committees;

developing and recommending corporate governance principles applicable to us;

overseeing the evaluation of management, the Board of Directors and the committees thereof; and

evaluating and recommending compensation for the Board of Directors.

The Corporate Governance and Nominating Committee will also consider properly submitted shareholder recommendations for candidates for membership on the Board of Directors as described below. In evaluating such recommendations, the Corporate Governance and Nominating Committee seeks to achieve a balance of knowledge, experience and capability on the Board of Directors and to address our director membership criteria. Any shareholder recommendations proposed for consideration by the Corporate Governance and Nominating Committee should include the candidate s name and qualifications for membership on the Board of Directors and should be addressed to:

Inter-Tel, Incorporated
1615 S. 52nd Street,
Tempe, Arizona 85281
Attn: Corporate Secretary.

The procedures for shareholder direct nomination of directors are described in detail in our bylaws, which will be provided to you upon written request. A report of the Corporate Governance and Nominating Committee is set forth below.

Director Qualifications

The Corporate Governance and Nominating Committee uses a variety of criteria to evaluate the qualifications and skills necessary for members of our Board of Directors. Under these criteria, members of the Board of Directors should have the highest professional and personal ethics and values, consistent with longstanding Inter-Tel values and standards. Director nominees should have broad experience at the policy-making level in business, government, education, technology or public interest. They should be committed to enhancing shareholder value and should have sufficient time to carry out their duties and to provide insight and practical wisdom based on experience. Their service on other boards of public companies should be limited to a number that permits them, given their individual circumstances, to perform responsibly all director duties. Each director must represent the interests of all shareholders.

Identifying and Evaluating Nominees for Director

The Corporate Governance and Nominating Committee utilizes a variety of methods for identifying and evaluating nominees for director. The Corporate Governance and Nominating Committee regularly assesses the appropriate size of the Board of Directors, and whether any vacancies on the Board of Directors are expected due to retirement or otherwise. In the event that vacancies are anticipated, or otherwise arise, the Corporate Governance and Nominating Committee will consider various potential candidates for director. Candidates may come to the attention of the Corporate Governance and Nominating Committee through current members of the Board of Directors, professional search firms, shareholders or other persons. These

candidates will be evaluated at regular or special meetings of the Corporate Governance and Nominating Committee, and may be considered at any point during the year. In evaluating the suitability of the candidates, the committee will consider relevant factors, including, among other things, issues of character, judgment, independence, age, expertise, diversity of experience, length of service, other commitments and the like. The committee will evaluate such factors, among others, and considers each individual candidate in the context of the current perceived needs of the board of directors as a whole.

As described above, the Corporate Governance and Nominating Committee will consider properly submitted shareholder recommendations for candidates for the Board of Directors. In evaluating such recommendations, the Corporate Governance and Nominating Committee will use the qualifications standards discussed above and seek to achieve a balance of knowledge, experience and capability on the Board of Directors.

The Board of Directors has final authority on determining the selection of director candidates for nomination to the Board. These policies and procedures may be modified at any time as may be determined by the committee.

Directors Standing for Election for the First Time

Director nominees Steven E. Karol, Robert Rodin and Norman Stout each were appointed by the Board after the 2005 annual meeting of shareholders in order to fill vacancies on the Board. The vacancies filled by the appointment of Messrs. Karol and Rodin were created by the resignation of Dr. Roland Haden from the Board and by a resolution to increase in the total number of directors to eight approved by the Board in February 2006. Mr. Stout was appointed as a member of the Board following a subsequent increase in the total number of directors in February 2006 to nine. In March 2006, Steven G. Mihaylo resigned from the Board and the total number of directors was reduced to eight. As a result, there presently are no vacancies on the Board.

Each of Messrs. Karol, Rodin and Stout has been nominated by the Corporate Governance and Nominating Committee for election at the annual meeting. Prior to becoming our Chief Executive Officer and a director, Mr. Stout was the Company s Executive Vice President, Chief Administrative Officer and Chief Strategy Officer. Messrs. Karol and Rodin were introduced to the Company and to the Corporate Governance and Nominating Committee by Mr. Cappello, the Chairman of the Board and an outside director. The Corporate Governance and Nominating Committee reviewed numerous candidates prior to nominating Messrs. Karol and Rodin for election to the Board. Mr. Stout was nominated in connection with his appointment as Chief Executive Officer.

Communications with the Board of Directors

Shareholders may communicate with the Board of Directors by submitting an email to financialinfo@inter-tel.com or by writing to us at Inter-Tel, Incorporated, Attention: Investor Relations, 1615 S. 52nd Street, Tempe, Arizona 85281. Communications received electronically or in writing will be distributed to the chairman of the board or the other members of the board as appropriate depending on the facts and circumstances outlined in the communication received.

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Board Attendance at Annual Shareholder Meetings

Although the Company does not have a formal policy regarding attendance by members of the board at the Company s annual meeting of shareholders, the Company encourages, but does not require, directors to attend. With the exception of Ms. Winkler, all of the Company s directors attended the 2005 annual meeting of shareholders.

Code of Business Conduct and Ethics

Inter-Tel has a Code of Business Conduct (***Code***) that applies to all of our employees, including our principal executive officer and principal financial and accounting officer. This code is posted on our Internet web site. The Internet address for our web site is http://www.inter-tel.com, and the code may be found as follows:

1. From our main web page at http://www.inter-tel.com, first click on Company.

2. Then click on About Inter-Tel .

3. Next, click on Code of Business Conduct.

We will provide a copy of the Code upon request made by email to financialinfo@inter-tel.com or by writing to us at Inter-Tel, Incorporated, Attention: Investor Relations, 1615 S. 52nd Street, Tempe, Arizona 85281. We intend to satisfy the disclosure requirement under Item 10 of Form 8-K regarding an amendment to, or waiver from, a provision of this Code by posting such information on our web site, at the address and location specified above, and to the extent required, by filing a Current Report on Form 8-K with the SEC disclosing such information.

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AUDIT COMMITTEE REPORT FOR THE YEAR ENDED DECEMBER 31, 2005

The Audit Committee oversees the Company s financial reporting process on behalf of the Board of Directors. Management has the primary responsibility for the financial statements and the reporting process including the systems of internal controls. In fulfilling its oversight responsibilities, the Audit Committee reviewed the audited financial statements in the Annual Report with management including a discussion of the quality, not just the acceptability, of the accounting principles, the reasonableness of significant accounting judgments and the clarity of the Company s disclosures in the financial statements.

In addition, the Audit Committee reviewed with the independent auditors, who are responsible for expressing an opinion on the conformity of those audited financial statements with accounting principles generally accepted in the United States, their judgments as to the quality, not just the acceptability, of the Company s accounting principles and such other matters as are required to be discussed with the Audit Committee under generally accepted auditing standards, and in particular, SAS 61. Furthermore, the Audit Committee discussed with the independent auditors the auditors independence from management and the Company including the matters in the written disclosures required by the Independence Standards Board Standard No. 1, and considered the compatibility of non-audit services with the auditors independence.

The Audit Committee also discussed with the Company s internal and independent auditors the overall scope and plans for their respective audits. At each regularly scheduled meeting, the Audit Committee meets with the internal auditors and independent registered public accounting firm, with and without management present, to discuss the results of their examinations, their evaluations of the Company s internal control, and the overall quality of the Company s financial reporting.

The Audit Committee held four (4) meetings during the fiscal year ended December 31, 2005. The members of the Audit Committee are Mr. Chapman (Chairman), Mr. Anderson, Mr. Cappello and Mr. Edens, all of whom meet the independence requirements of the Nasdaq stock market. Mr. Cappello joined the Audit Committee on October 17, 2005. Dr. Roland Haden was a member of the Audit Committee through July 22, 2005 and met the independence requirements of the Nasdaq stock market during his tenure. The Board has determined that Mr. Chapman is an Audit Committee financial expert.

Non-management directors meet regularly in executive sessions without management. Non-management directors are all those who are not Company officers. An executive session is held in conjunction with each regularly scheduled Board meeting and other sessions may be called by directors in their discretion or at the request of the Board.

In reliance on the reviews and discussions referred to above, the Audit Committee recommended to the Board of Directors, and the Board approved, that the audited financial statements be included in the Annual Report on Form 10-K for the year ended December 31, 2005 for filing with the Securities and Exchange Commission. The Audit Committee has also appointed, subject to shareholder ratification, Ernst & Young LLP, as the Company s independent registered public accounting firm.

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AUDIT COMMITTEE:

Jerry W. Chapman (Chairman),
J. Robert Anderson,
Alexander Cappello and
Gary Edens.
February 13, 2006

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COMPENSATION COMMITTEE REPORT FOR THE YEAR ENDED DECEMBER 31, 2005

Executive Compensation Principles

The Company s Compensation Committee s responsibilities include determining the cash and non-cash compensation of executive officers. The Compensation Committee s policy regarding compensation of the Company s executive officers is to provide generally competitive salary levels and compensation incentives in order to attract and retain individuals of outstanding ability; to recognize and reward individual performance and the performance of the Company; and to support the Company s primary goal of increasing shareholder value. Through 2005, except as noted in Certain Other Benefits below, non-cash compensation had been limited to stock option grants to purchase Common Stock at fair market value at the grant date and other perquisites. All executive officers and certain employees of the Company have participated in such stock incentive plans. All options to purchase Common Stock were granted with exercise prices equal to the fair market value of the Common Stock on the date of grant. These plans are designed to attract and retain qualified personnel and to tie their performance to the enhancement of shareholder value. Stock options vest at the end of either four or five years from the date of grant.

Executive officers, together with other permanent Inter-Tel employees, may also participate in the Company s 401(k) Thrift Savings Plan. All executive officers may also participate in the Inter-Tel Employee Stock Purchase Plan except for Mr. Mihaylo, who is not eligible to participate because he owns greater than 5% of the Company s Common Stock. Please refer to the Summary Compensation Table below for additional information.

Executive Compensation Program for Key Executives

The total compensation program for executives includes both cash and equity-based compensation. The Compensation Committee determines the level of salary for executive officers and determines the salary or salary ranges based upon periodic reviews of base salary levels for comparable officer positions in similar companies of comparable size. Salary changes are based upon comparable market rates, the Compensation Committee s assessment of the executive s performance, and the scope and complexity of the position held.

At the beginning of 2005, the Compensation Committee considered the Company s target earnings per share goals and the operating plans of the Company. Consideration included past and anticipated performance, new product and market expectations, assets employed and similar factors. The Compensation Committee set earnings per share performance levels for the consolidated Company, upon which incentives were established for each of the executives. Cash bonus awards, based upon meeting or exceeding such performance levels (limited to a maximum percentage of base salary), were set for each executive officer. With the exception of Mr. Ford, Named Executive Officer bonuses were based entirely on Inter-Tel earnings per share targets. Two-thirds (2/3) of the performance award opportunity for Mr. Ford was based on earnings and other specific measurements within his operating segment of the Company, and one-third (1/3) was based on Inter-Tel earnings per share targets. Maximum bonus awards as a percentage of annual base compensation were set for the Named Executive Officers, as follows:

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Officer	Maximum 2005 Bonus Award (as a percentage of annual base compensation)
Steven G. Mihaylo	125%
Craig W. Rauchle	100%
Norman Stout	100%
Jeffrey T. Ford	100%
Kurt R. Kneip	60%

For 2005, bonus goals based on earnings per share calculations excluded the impact of in-process research and development charges incurred in connection with acquisitions, to the extent applicable. In addition, the Committee is authorized to use its discretion to revise the calculated bonus amounts upwards or downwards based on any information the Committee deems appropriate.

The cash bonuses in the Summary Compensation Table reflect the performance of the Named Executive Officers against the targets established at the beginning of each year. No bonuses were earned in connection with earnings per share goals for 2005, although Mr. Ford earned a bonus of $14,261 based on measurements within his operating segment of the Company.

The Company granted stock options to 3 of the 5 Named Executive Officers during the year ended December 31, 2005. Refer to Option Grants in Last Fiscal Year table for additional information.

Certain Other Benefits

To remain competitive in the market for a high caliber management team, Inter-Tel provides some of its executive officers, including the CEO, with certain fringe benefits, including a car allowance, 401(k) match, selected reimbursement of club dues, selected use of Inter-Tel telephone systems in the home and business use of corporate aircraft. During 2005, $7,938 was included in Mr. Rauchle s income in connection with travel costs incurred by him and his guest for attendance at company-sponsored business trips. In addition, during 2003, Mr. Rauchle received other compensation related to reimbursement of health and welfare benefits for a family member. The Committee periodically reviews fringe benefits made available to the Company s executive officers, including the CEO. For additional information regarding fringe benefits made available to the Company s executive officers, please see Summary Compensation Table.

Chief Executive Officer

The Chief Executive Officer s salary for 2005 was determined based upon a review of the salaries of Chief Executive Officers of similar companies of comparable size and capitalization and upon a review of the Chief Executive Officer s performance compared with the prior year and the 2004 budget. The Compensation Committee determined that the CEO s 2005 maximum bonus opportunity should increase to 125% of base salary compared to 100% of base salary in

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prior years. For 2006, the Compensation Committee determined that the CEO s 2006 target bonus opportunity should be 100% of base salary, with a maximum bonus opportunity of 150% of base salary. No stock options were granted to Mr. Mihaylo to purchase Inter-Tel stock during 2005.

COMPENSATION COMMITTEE:
J. Robert Anderson (Chairman) and
Agnieszka Winkler
February 13, 2006

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GOVERNANCE AND NOMINATING COMMITTEE REPORT FOR THE YEAR ENDED DECEMBER 31, 2005

The Corporate Governance and Nominating Committee is composed of four directors, all of whom meet the Nasdaq director independence standards. The Committee operates under a written charter adopted by the Board of Directors. A copy of the Charter was filed with our proxy dated March 18, 2004 and this proxy may be found on Inter-Tel s website at http://www.inter-tel.com.

Composition of Board of Directors/ Nominees

The Committee recommends to the Board the nominees for all directorships to be filled by the Board. The Committee also reviews and makes recommendations to the Board on matters such as the size and composition of the Board in order to ensure the Board has the requisite expertise and its membership consists of persons with sufficiently diverse and independent backgrounds. Between annual shareholder meetings, the Board may elect directors to vacant Board positions to serve until the next annual meeting.The Board proposes a slate of nominees for election to the Board at the annual meeting. Shareholders may also propose nominees (other than self-nominations) for consideration by the Committee by submitting the names, qualifications and other supporting information to: Secretary, Inter-Tel, Incorporated, 1615 S. 52nd Street, Tempe, AZ 85281. Properly submitted recommendations must be received at the Company s principal executive offices not less than 120 calendar days before the date of the Company s proxy statement released to shareholders in connection with the previous year s annual meeting, to be considered by the Committee for inclusion in the following year s nominations for election to the Board. Properly submitted candidates will be evaluated in the same manner as those candidates recommended by other sources. All candidates are considered in light of the needs of the Board with due consideration given to the qualifications described below.

Qualifications

The Committee considers several qualifications when considering candidates for the Board. Among the most important qualities directors should possess are the highest personal and professional ethical standards, integrity and values. Candidates should be committed to representing the long-term interests of all of the shareholders. Directors must also have practical wisdom and mature judgment. Directors must be objective and inquisitive. Directors must be willing to devote sufficient time to carrying out their duties and responsibilities effectively, and should be committed to serve on the Board for an extended period of time. Directors should also be prepared to offer their resignation in the event of any significant change in their personal circumstances that could affect the discharge of their responsibilities as directors of the Company, including a change in their principal job responsibilities.

Identification of Directors

The Committee conducts all necessary and appropriate inquiries into the backgrounds and qualifications of possible candidates as directors. It has the sole authority to retain and terminate

any search firm to be used to assist it in identifying and evaluating candidates to serve as directors of the Company.

The Committee identifies candidates through a variety of means, including search firms, recommendations from members of the Committee and the Board, including the Chairman and Chief Executive Officer, and suggestions from Company management. The Committee performs interviews of candidates for further consideration for election to the Board of Directors, and may invite member of management or others to join in such interviews. Upon the recommendation of the Committee, prospective board members are nominated to the Board of Directors for election the Company s Annual Meeting of Shareholders, or earlier if approved by the Board of Directors.

Corporate Governance and the Code of Business Conduct

The Committee reviews management s monitoring of compliance with the Company s Code of Business Conduct. In addition, the Committee has established a process for shareholders to send communications to the Board, as outlined in the Code of Business Conduct, which may be found on the Company s website at www.inter-tel.com. See the Corporate Governance section below for more information on our corporate governance practices.

Corporate Governance and Nominating
Committee:
Gary D. Edens (Chairman),
Alexander Cappello,
Jerry Chapman and
Agnieszka Winkler.
February 13, 2006

Corporate Governance

Inter-Tel has operated under sound corporate governance practices for many years. We believe it is important to disclose to shareholders a summary of our major corporate governance practices. Some of these practices have been in place for many years. Others have been adopted in response to regulatory and legislative changes. We will continue to assess and refine our corporate governance practices and share them with you.

Director Independence

A majority of the directors must be independent directors under the Nasdaq rules. The Nasdaq rules provide that no director can qualify as independent unless the Board affirmatively determines that the director has no material relationship with the listed company. The Board has adopted the Nasdaq standards in determining whether or not a director has a material relationship with the Company:

Based on these independence standards and all of the relevant facts and circumstances, the Board determined that, with the exception of Steven G. Mihaylo, all directors are considered independent.

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Committee Charters/ Codes of Ethics

The Company has published in public filings listed on its website (inter-tel.com) the Charter of each of the Audit, Compensation, and Corporate Governance and Nominating Committees of the Board, as well as its Code of Business Conduct, which apply to all officers and employees. Any waiver of, or amendments to, the codes of ethics for directors or executive officers, including the chief executive officer and the chief financial officer must be approved by the Board of Directors and would be posted on the Company s website within four business days of any such waiver or amendment. Copies of each of the committee charters and the codes of ethics referred to above are also available by writing to our Investor Relations Department, 1615 S. 52nd Street, Tempe AZ 85281.

Executive Sessions of Non-Employee Directors

Independent directors ordinarily meet in executive session without management present at regularly scheduled Board meetings and may meet at other times at the discretion of the presiding independent director or at the request of any non-employee director. Jerry Chapman, an independent director, financial expert and Chairman of the Audit Committee, is the presiding independent director for the executive sessions of non-management directors. Additionally, all of the independent directors meet at least once annually without management or non-independent directors present.

Audit Committee

The Charter of the Audit Committee provides that a member of the Audit Committee generally may not serve on the audit committee of more than two other public companies. The Board has designated Jerry W. Chapman as an Audit Committee financial expert. Mr. Chapman meets the independence standards for audit committee members under the Nasdaq and SEC rules. The lead partner of the Company s independent public accountants is rotated at least every five years.

Board Committees

Only independent directors serve on the Audit, Compensation and Corporate Governance and Nominating Committees, in accordance with the independence standards of the Nasdaq rules and the Company s Corporate Governance Principles. The Board, and each committee of the Board, has the authority to engage independent consultants and advisors at the Company s expense.

Communications with the Board / Annual Meeting Attendance

The Board has established a process by which shareholders may send communications to the Board. For a description of the manner in which you can send communications to the Board, please visit the Company s website (www.inter-tel.com). All members of the Board are requested to attend the annual meeting, unless unusual circumstances would prevent such attendance. All directors who were then members of the Board attended last year s annual meeting.

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COMPARISON OF FIVE-YEAR CUMULATIVE TOTAL RETURNS

The following graph compares the cumulative total return of the Company s Common Stock with the Nasdaq U.S. Index and the Nasdaq Telecommunications Stocks index from December 2000 to December 2005. Inter-Tel selected the Nasdaq Telecommunications Stock index for comparisons in this second graph and for future comparative periods.

COMPARISON OF CUMULATIVE TOTAL RETURNS AMONG INTER-TEL, NASDAQ U.S. AND NASDAQ TELECOM INDICES

Legend

Description	12/29/00	12/31/01	12/31/02	12/31/03	12/31/04	12/30/05
INTER-TEL, INCORPORATED	100.0	250.97	274.44	330.52	366.05	276.53
Nasdaq U.S.	100.0	79.32	54.84	81.99	89.22	91.12
Nasdaq Telecommunications Stocks: (SIC 4800-4899 US & Foreign)	100.0	66.54	30.63	50.94	54.32	51.61

Notes: A. The lines represent monthly index levels derived from compounded daily returns that include all dividends. B. The indexes are re-weighted daily, using the market capitalization on the previous trading day. C. If the monthly interval, based on the fiscal year-end, is not a trading day, the preceding trading day is used. D. The index level for all series was set to $100.0 on 12/29/00.

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EQUITY COMPENSATION PLAN INFORMATION

The following table summarizes our equity compensation plan information as of December 31, 2005. Information is included for both equity compensation plans approved by Inter-Tel shareholders and equity compensation plans not approved by Inter-Tel shareholders.