Mt. Angel Telephone Company

Financial Statements

Years Ended December 31, 2014 and 2013

AKT
CPAs AND BUSINESS CONSULTANTS

MT. ANGEL TELEPHONE COMPANY

Financial Statements

Years Ended December 31, 2014 and 2013

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors
Mt. Angel Telephone Company
Mt. Angel, Oregon

We have audited the accompanying financial statements of Mt. Angel Telephone Company (the Company), which compromise the balance sheets as of December 31, 2014 and 2013, and the related statements of operations, comprehensive income, changes in stockholder's equity, and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements
Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility
Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Mt. Angel Telephone Company as of December 31, 2014 and 2013, and the results of its operations and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

AKT LLP

Salem, Oregon
March 20, 2015

MT. ANGEL TELEPHONE COMPANY

Balance Sheets

December 31, 2014 and 2013

ASSETS	2014	2013
Current Assets:		
Cash and cash equivalents	$ 481,241	$ 887,795
Marketable securities	103,011	50,317
Accounts receivable, less allowance for doubtful accounts of zero	233,685	248,143
Materials and supplies	39,058	36,493
Income taxes receivable	129,570	-
Prepaid expenses	32,978	35,085
Total Current Assets	1,019,543	1,257,833
Other Assets and Investments:		
Other assets	1,489	1,794
Investments	44,019	42,323
Total Other Assets and Investments	45,508	44,117
Noncurrent Deferred Income Tax Asset	712,000	878,000
Property, Plant, and Equipment:		
In service	6,527,048	6,018,191
Less accumulated depreciation	4,933,037	4,697,472
Property, Plant, and Equipment, net	1,594,011	1,320,719
	$ 3,371,062	$ 3,500,669

See accompanying notes to financial statements.

LIABILITIES AND STOCKHOLDER'S EQUITY	2014	2013
Current Liabilities:		
Current portion of long-term debt	$ 189,625	$ 304,500
Accounts payable	106,219	79,048
Income taxes payable	-	38,710
Accrued expenses	25,338	27,945
Advanced billings	82,899	107,557
Current deferred income tax liability	25,900	42,000
Total Current Liabilities	429,981	599,760
Long-term Liabilities		
Other liabilities	101,380	103,698
Long-term debt	-	189,625
Intercompany note payable	800,000	800,000
Total Long-Term Liabilities	901,380	1,093,323
Total Liabilities	1,331,361	1,693,083
Stockholder's Equity:		
Common stock of $3.125 par value; authorized 4,800 shares, 1,737.21 of shares issued and outstanding	5,429	5,429
Additional paid in capital	30,846	30,846
Retained earnings	2,005,353	1,770,994
Accumulated other comprehensive income (loss)	(1,927)	317
Total Stockholder's Equity	2,039,701	1,807,586
	$ 3,371,062	$ 3,500,669

See accompanying notes to financial statements.

MT. ANGEL TELEPHONE COMPANY

Statements of Operations

Years Ended December 31, 2014 and 2013

	2014	2013
Operating Revenues:		
Local network	$ 348,051	$ 405,673
Network access	1,173,228	1,291,132
Internet	334,475	288,968
Miscellaneous	192,639	185,516
Total Operating Revenues	2,048,393	2,171,289
Operating Expenses:		
Plant specific	431,823	416,289
Plant nonspecific	120,502	140,520
Customer	309,441	334,981
Corporate	251,430	181,344
Depreciation	235,567	208,638
Total Operating Expenses	1,348,763	1,281,772
Operating Taxes:		
Operating income taxes	132,641	248,900
Other operating taxes	46,413	41,174
Total Operating Expense and Taxes	1,527,817	1,571,846
Operating Income	520,576	599,443
Other Income (Expense):		
Investment income	14,137	14,464
Non-regulated income	143,776	170,167
Non-regulated expense	(389,595)	(316,817)
Total Other Expense, net	(231,682)	(132,186)
Income Available for Fixed Charges	288,894	467,257
Fixed Charges - interest on long-term debt	54,535	72,970
Net Income	$ 234,359	$ 394,287

See accompanying notes to financial statements.

MT. ANGEL TELEPHONE COMPANY

Statements of Comprehensive Income

Years ended December 31, 2014 and 2013

	2014	2013
Net Income	$ 234,359	$ 394,287
Other Comprehensive Income		
Unrealized holding gains (losses) on marketable securities	(2,922)	1,659
Relcassifications for realized gains included in net income	(722)	(1)
Deferred tax asset on unrealized loss	1,400	-
Total Other Comprehensive Income (Loss)	(2,244)	1,658
Total Comprehensive Income	$ 232,115	$ 395,945

See accompanying notes to financial statements.

MT. ANGEL TELEPHONE COMPANY

Statements of Changes in Stockholder's Equity

Years Ended December 31, 2014 and 2013

	Common Stock	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance, December 31, 2012	$ 5,429	$ 30,846	$ 1,376,707	$ (1,341)	$ 1,411,641
2013 Net Income	-	-	394,287	-	394,287
2013 Other Comprehensive Income	-	-	-	1,658	1,658
Balance, December 31, 2013	5,429	30,846	1,770,994	317	1,807,586
2014 Net Income	-	-	234,359	-	234,359
2014 Other Comprehensive loss	-	-	-	(2,244)	(2,244)
Balance, December 31, 2014	$ 5,429	$ 30,846	$ 2,005,353	$ (1,927)	$ 2,039,701

See accompanying notes to financial statements.

MT. ANGEL TELEPHONE COMPANY

Statements of Cash Flows

Years Ended December 31, 2014 and 2013

	2014	2013
Cash Flows from Operating Activities:		
Net income	$ 234,359	$ 394,287
Adjustments to reconcile net margin to net cash provided by operating activities:		
Depreciation	235,567	208,638
Change in deferred taxes	151,300	137,500
Gains on investments and marketable securities	(2,418)	(2,461)
Changes in assets and liabilities:		
Accounts receivable	14,458	(102,862)
Materials and supplies	(2,565)	20,662
Income taxes receivable	(129,570)	(27,520)
Prepaid expenses	2,107	(15,359)
Accounts payable	27,171	14,321
Income taxes payable	(38,710)	38,710
Accrued expenses	(2,607)	(21,492)
Advanced billings	(24,658)	107,557
Other liabilities	(2,318)	(57,505)
Net Cash Provided by Operating Activities	462,116	694,476
Cash Flows from Investing Activities:		
Purchases of property, plant, and equipment	(508,859)	(333,130)
Proceeds from sales and maturities of marketable securities	102,244	65,200
Purchases of marketable securities	(157,860)	(17,142)
Change in other assets	305	356
Net Cash Used by Investing Activities	(564,170)	(284,716)
Cash Flows from Financing Activities: Payments on long-term debt	(304,500)	(304,500)
Net Increase (Decrease) In Cash and Cash Equivalents	(406,554)	105,260
Cash and Cash Equivalents, beginning	887,795	782,535
Cash and Cash Equivalents, ending	$ 481,241	$ 887,795
Cash Paid During the Year for Interest	$ 54,535	$ 72,970
Cash Paid During the Year for Taxes	$ 149,621	$ 100,210

See accompanying notes to financial statements.

Note 1 - Organization and Summary of Significant Accounting Policies

Organization
Mt. Angel Telephone Company (the Company) is an Oregon corporation providing telecommunications, broadband services within and around the city of Mt. Angel, Oregon. The Company is a wholly-owned subsidiary of Canby Telephone Association (CTA).

Basis of Accounting
The Company's financial statements are prepared on the accrual basis of accounting in conformity with the accounting principles generally accepted in the United States of America applicable to regulated enterprises.

Regulation
The Company is subject to limited regulation by the Oregon Public Utility Commission (PUC) and Federal Communications Commission (FCC). The Company maintains its accounting records in accordance with the Uniform System of Accounts, as prescribed by the FCC, and adopted by the PUC. As a result, the application of accounting principles generally accepted in the United States of America by the Company differs in certain respects from the application by non-regulated entities. Such differences primarily concern the time at which certain items enter into the determination of net income.

Regulatory and legislative actions, as well as future regulations, could have a significant impact on the Company's future operations and financial condition. See Note 1, National Broadband Plan and FCC Order.

Estimates
The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses. Actual results could differ from those estimates.

Comprehensive Income
The Company reports comprehensive income. The purpose of reporting comprehensive income is to report all changes in equity of an enterprise that result from recognized transactions and other economic events of the period other than transactions with owners in their capacity as owners.

Income Taxes
The Company is a taxable C corporation.

Income taxes are provided for the tax effects of transactions reported in the financial statements and consist of taxes currently due and deferred income taxes. Deferred taxes represent the future tax return consequences of differences between the financial statement and the tax basis of assets and liabilities, which will either be taxable or deductible when the related assets or liabilities are recorded or settled.

The Company follows accounting standards generally accepted in the United States of America related to the recognition of uncertain tax positions. The Company recognizes accrued interest and penalties associated with uncertain tax positions as part of the income tax provision, when applicable. There were no amounts accrued in the financial statements related to uncertain tax positions.

The Company files federal, state and local income tax returns. With limited exceptions, the Company is no longer subject to examinations for years before 2011.

Note 1 - Organization and Summary of Significant Accounting Policies, continued

Revenue Recognition
The Company recognizes revenues when earned regardless of the period in which they are billed.

Monthly service fees derived from local telephone and broadband service are billed in advance. Advance billings are recorded as a liability and subsequently transferred to income in the period earned. Access charges (see Note 1, Network Access Revenue), long distance, and other revenues based on usage are billed in arrears.

Cash and Cash Equivalents
The Company considers all highly liquid investment securities with a maturity of 3 months or less to be cash equivalents. The Company maintains its cash in bank deposit accounts that are insured by the Federal Deposit Insurance Corporation (FDIC) up to a limit of $250,000 per depositor. At December 31, 2014 the Company had $80,366 in uninsured cash ($454,107 at December 31, 2013).

The Company has not experienced any losses in such accounts and believes it is not exposed to any significant credit risk on cash.

Accounts Receivable
The Company extends credit to its customers. Credit risk associated with receivables is periodically reviewed by management and, if required, an allowance for doubtful accounts is established. Receivables from subscribers are due 30 days after the issuance of the invoice. Receivables from other exchange carriers are typically outstanding from 30 to 60 days before payment is received. Delinquent accounts are written off to uncollectible expense when it is determined that the account will not be collected. Receivables past due more than 90 days are considered delinquent.

Materials and Supplies
Materials and supplies are stated at the lower of cost or market. Cost is determined principally by the average cost method.

Fair Value of Financial Instruments
The Company's financial instruments, none of which are held for trading purposes, include cash and cash equivalents, marketable securities, receivables, accounts payable, and notes payable. The Company estimates that the fair value of all of these non-derivative financial instruments at December 31, 2014 and 2013 does not differ materially from the aggregate carrying value of its financial instruments recorded in the accompanying balance sheets.

Marketable Securities
The Company has classified all marketable securities as available for sale. These investments are stated at fair value in the financial statements with accumulated unrealized gains and losses reported as a separate component of stockholder's equity.

Property, Plant, and Equipment
Property, plant, and equipment in service and under construction is stated at cost, including estimated overhead expense. Depreciation is calculated on a straight-line basis over the estimated life of the classes of property and equipment in accordance with rates consistent with industry standards, and range from 2.5% to 33.33%. Expenditures for maintenance and repairs are charged to expense as incurred and major additions are capitalized. Costs of plant retired are eliminated from utility plant accounts, and such costs plus removal expenses, less salvage, are charged to accumulated provision for depreciation in accordance with industry practice.

Note 1 - Organization and Summary of Significant Accounting Policies, continued

Network Access Revenues

Network access revenue is received under a system of access charges. Access charges represent a methodology by which local telephone companies, including the Company, charge the long-distance carrier for access and interconnection to local facilities. The Company has elected to file access tariffs through the National Exchange Carriers Association (NECA) and directly with the PUC for these changes. These access tariffs are subject to approval by the FCC for interstate charges and the PUC for intrastate charges.

When network access revenues have been received pursuant to the settlement and access agreements above, they are then either placed into a common pooling arrangement with other exchange carriers for redistribution or kept by the Company. The redistributions are made according to formulas established by the governing boards of the pools and are generally based upon expenses incurred and investments maintained.

The Cooperative participates in pooling arrangements with NECA. They also participated in pooling arrangements with OECA through July 2013, at which time the OECA Optional pool closed.

Settlement, access, and pool distribution revenues are recorded when the amounts become determinable. Related expenses are recorded when incurred. Subsequent true-ups and retroactive adjustments, which are generally allowed for a period up to 24 months (NECA pool only), are recorded in the year in which such adjustments become determinable.

In 2014, the Company received $611,939 ($740,727 in 2013) in interstate access revenues administered through the NECA pool. In 2014, the Company received $349,016 from the Oregon Universal Service Fund ($341,755 in 2013). The current funding levels for the Oregon Universal Service Fund are determined in accordance with PUC Order 13-162 which ends June 30, 2016. The level of funding after this date can not be reasonably estimated at this time.

National Broadband Plan and FCC Order

In 2010 the FCC issued the National Broadband Plan which outlined a long-term plan to increase broadband penetrations and services throughout the United States of America. The plan further outlined a proposed long-term phase-out of access charges (referred to as Intercarrier Compensation) and moved to support mechanisms based on broadband services rather than the current Universal Service High Cost Loop Fund administered by USAC.

In response to the plan, the FCC on October 27, 2011, approved Report and Order 11-161 (the Order), that begins the process of reforming the universal service and intercarrier compensation (ICC) systems and adopts support for broadband-capable networks as an express universal service principle. The Order further creates the Connect America Fund which will ultimately replace all existing high-cost support mechanisms as well as help facilitate ICC reforms.

Note 1 - Organization and Summary of Significant Accounting Policies, continued

National Broadband Plan and FCC Order, continued
The key provisions of the order include;

- Capping the federal universal service fund at current levels.
- Placing limitations on capital and operating spending.
- Establishing local rate benchmarks.
- Capping the per-line support amount for the universal service high cost loop fund at $250 per month.
- Phase out of local switching support and the establishment of the CAF for recovery of investment and expenses related to the provision of switching services.
- Reforming the ICC system by adopting a plan to transition from access charges to a bill and keep framework. The transition period for rate-of-return carriers such as the Company is approximately 9 years from the date of the order.
- Adoption of a monthly Access Recovery Charge as a transitional recovery mechanism to mitigate the impact of reduced intercarrier revenues.

The Order was effective December 29, 2011 and implementation began July 1, 2012. As of the implementation date CAF recovery is calculated based on the frozen fiscal year 2011 interstate switched access revenue requirement, plus certain 2011 intrastate access revenues, and will decline annually by 5% during the transition period.

In 2014 the FCC issued Orders for Reconsideration that included provisions to eliminate the quantile regression benchmarking analysis (this removes the limitations on capital spending contained in the Order), reinstate the safety-net additive that was eliminated as part of the Order and continued the transition of the local rate benchmark.

As of December 31, 2014 the Company is transitioning its local rates and meets the local rate benchmark requirements. The Company is not subject to the $250 per line support cap. Furthermore, for the period ended December 31, 2014 the impacts to the Company related to the 5% annual decline in switched access revenues have not been significant.

The overall reform process will take place in phases and will take several years to implement. Furthermore, the Order includes a Further Notice of Proposed Rulemaking, the FCC has issued numerous Orders for Reconsideration and continues to seek comments on various items. As a result, the ultimate outcome of these proceedings and their impact is uncertain at this time.

Subsequent Events
The Company has evaluated subsequent events through March 20, 2015, which is the date the financial statements were available to be issued.

Note 2 - Investments

Investments are recorded at cost and consist of the following:

	2014	2013
CoBank, equity investment and patronage allocations	$ 44,019	$ 42,323

CoBank is a cooperative bank. Borrowers are required to invest a minimum of $1,000 or 2% of their loan, whichever is less. Patronage dividends are paid annually in cash and in stock at the discretion of the board of directors of CoBank.

Note 3 - Marketable Securities

As mentioned in Note 1, at December 31, 2014 and 2013 marketable securities have been categorized as available for sale and are stated at fair value in the financial statements, with unrealized gains and losses included in comprehensive income as a separate component of stockholder's equity.

The Company adopted a hierarchal disclosure framework, which among other matters requires enhanced disclosure about investments that are measured and reported at fair value. This framework prioritizes and ranks the level of market price observability used in measuring investments at fair value. The Company's marketable securities are measured and reported at fair value on a recurring basis based on quoted prices available in active markets for identical investments as of the reporting date (Classification Level 1). There have been no changes in the methodologies used at December 31, 2014 and 2013.

At December 31, the Company's securities consisted of the following:

	2014	2013
Fair Value:		
Municipal Bonds	$ 19,881	$ 50,317
Mutual Funds	83,130	-
Total Fair Value	$ 103,011	$ 50,317
Cost	$ 106,338	$ 50,000
Gross unrealized holding gains (losses)	$ (3,327)	$ 317

Gross unrealized holding loss of $3,327 (unrealized holding gain of $317 in 2013) are included in accumulated other comprehensive income, net of deferred taxes of $1,400 in 2014 (none in 2013). Proceeds from the sale of marketable securities for the year ended December 31, 2014 were $102,244 ($65,200 in 2013) with realized gain of $722 for the year ended December 31, 2014 ($1 gain in 2013). The Company uses the specific identification method to determine the cost of securities sold.

Included in marketable securities at December 31, 2014 are debt securities available for sale with maturities as follows:

	Amortized Cost	Fair Value
Amounts maturing in:		
One year or less	$ 20,471	$ 19,881
	$ 20,471	$ 19,881

Note 4 - Property, Plant, and Equipment

Listed below are the major classes of property, plant, and equipment in service:

	2014	2013
Land and support	$ 1,068,270	$ 1,058,647
Central office	3,031,228	2,630,713
Cable and wire facilities	2,427,550	2,314,402
Under construction	-	14,429
	$ 6,527,048	$ 6,018,191

Note 5 - Long-Term Debt

Long-term debt consists of the following:

	2014	2013
Note payable to CoBank, at 5.72% at December 31, 2014 and 2013, payable in level quarterly principal only installments of $76,125, interest payable monthly, collateralized by substantially all real and personal property, due in 2015.	$ 1,068,270	$ 494,125
3.75% intercompany note payable to DirectLink, with interest only payments until the final payment of the full balance, due July 1, 2019.	800,000	800,000
	989,625	1,294,125
Less current portion	189,625	304,500
	$ 800,000	$ 989,625

Future maturities of long-term debt are as follows:

2015	$ 189,625
2016	-
2017	-
2018	-
2019	800,000
	$ 989,625

The long-term debt agreement contains restrictions on the payment of dividends and redemption of capital stock. The terms of the long-term debt agreement also require the maintenance of defined amounts of stockholder's equity and certain financial ratios. Management believes the Company was in compliance with the terms of the debt agreement for the years ended December 31, 2014 and 2013.

Note 6 - Pension Plan

Effective January 1, 2013, all employees of the Company were transferred to their parent Company, CTA. As a result, all employee and employer contributions into the Company’s 401(k) profit sharing plan (the Plan) ceased as of that date. Effective January 15, 2015 the plan was terminated.

Note 7 - Other Liabilities

The Company sponsors a non-qualified, defined benefit, post-retirement benefit plan which provides certain health care benefits for retired employees and their respective spouses until the date of the retired employee's death. Benefits are based on years of service and the employee's average compensation for the five highest years of employment.

The annual measurement date is December 31 for the post-retirement benefit plan. The following tables provide information about changes in the benefit obligation and plan assets and the funded status of the Company's post-retirement benefit plan.

		2014		2013
Benefit obligation at December 31	$	114,000	$	117,000
Fair value of plan assets at December 31		-		-
Net unfunded status of the plan	$	(114,000)	$	(117,000)
Benefit payments	$	(12,620)	$	(12,620)
Long-term benefit obligation	$	(114,000)	$	(117,000)
Other post-employment obligations		-		682
		(114,000)		(116,318)
Less current portion		12,620		12,620
	$	(101,380)	$	(103,698)

Assumptions

Weighted average assumptions used in the accounting for the Company's post-retirement benefit plan were:

	2014	2013
Weighted-average assumptions used to determine benefit obligations at December 31:	5.75%	5.75%
Weighted average assumptions used to determine net periodic benefit cost for years ended December 31:	5.75%	5.75%

Cash Flows

The Company does not expect to contribute to its post-retirement benefit plan in 2015.

Post-retirement Benefit

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

2015	$	12,620
2016		12,620
2017		12,620
2018		12,620
2019		12,620
Years 2020 - 2024		63,105

Note 8 - Income Taxes

The following is a summary of the significant components of the Company's deferred tax assets and liabilities as of December 31:

	2014	2013
Current:		
Accrual to cash adjustment	$ (30,000)	$ (42,000)
Unrealized loss on marketable securities	1,400	-
State net operating losses	2,700	-
Current deferred income tax liability	$ (25,900)	$ (42,000)
Noncurrent:		
Property, plant and equipment, depreciation	$ 673,000	$ 838,000
Post-retirement health benefits accrual	39,000	40,000
Noncurrent deferred income tax asset	$ 712,000	$ 878,000

Income tax expense for the years ended December 31 consists of the following:

	2014	2013
Prior year over accrual	$ (1,359)	$ (2,260)
Current provision	(17,300)	113,660
Deferred tax position	151,300	137,500
Income tax expense	$ 132,641	$ 248,900

The provision for income taxes differs from the amount computed by applying the current statutory federal and state income tax rates to earnings before income taxes due to the effects of state taxes, nondeductible items, prior year over or under accruals, and the use of accelerated depreciation for income tax purposes.

Note 9 - Related Party

The Company is a reseller of internet services provided by CTA. For the year ended December 31, 2014 internet expense to CTA was $99,681 ($124,861 in 2013). Effective January 1, 2013 the Company transferred all of their employees to CTA. The Company is charged for all of the labor, benefits and overhead costs that CTA provides on behalf of the Company and for the year ended December 31, 2014 total costs were $598,061 ($486,659 in 2013). At December 31, 2014 there were payables of $87,918 to CTA ($64,632 in 2013).

On July 1, 2009, the Company entered into a debt agreement with Direct Link of Oregon, Inc. (DLO), a wholly-owned subsidiary of CTA, for $800,000. Interest expense for the year ended December 31, 2014 was $30,000 ($30,000 at December 31, 2013). See Note 4 for further details.

On September 1, 2012, the Company entered into a rental agreement for the use of their office building with Consolidated Business Services, LLC (CBS) a management and accounting service company whom the Company's Parent company, CTA, is a one-third owner. The Company received rental payments of $7,000 during 2014 ($21,000 in 2013). During 2014, CBS moved out of the building. CBS provided accounting and regulatory services to the Company in the amount of $109,386 in 2014 (120,259 in 2013). At December 31, 2014 there were payables to CBS of $9,116 which are included in the amount owed to CTA above ($7,307 in 2013).