

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES

REPORT ON AUDIT OF CONSOLIDATED FINANCIAL
STATEMENTS AND ADDITIONAL INFORMATION

For the Years Ended
December 31, 2014 and 2013

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Duo County Telephone Cooperative Corporation, Inc.
Jamestown, Kentucky 42629

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Duo County Telephone Cooperative Corporation, Inc., and subsidiaries which comprise the consolidated balance sheets as of December 31, 2014 and 2013, and the related statements of income, comprehensive income, patronage capital and other equities 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 consolidated 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 consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these consolidated financial statements based on our audit. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 opinions.

Opinions

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the respective financial position of Duo County Telephone Cooperative Corporation, Inc. and subsidiaries as of December 31, 2014 and 2013, and the results of its operations and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 26, 2015, on our consideration of the Duo County Telephone Cooperative Corporation, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Duo County Telephone Cooperative Corporation, Inc.'s internal control over financial reporting and compliance.

Campbell, Myers & Rutledge, PLLC

Certified Public Accountants

March 26, 2015

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
BALANCE SHEETS
December 31, 2014 and 2013

ASSETS

	<u>2014</u>	<u>2013</u>
Current assets		
Cash and cash equivalents	\$ 3,663,380	\$ 3,571,650
Temporary cash investments	4,360,290	3,767,871
Cash, RUS construction fund	203	35,547
Marketable Securities	3,509,198	3,112,602
Accounts receivable, less allowance for doubtful accounts of \$54,189 in 2014 and \$54,189 in 2013.	1,534,186	1,573,215
Materials and supplies at average cost which is less than market	2,191,254	2,199,693
Accrued interest receivable	200,003	100,253
Prepaid expenses	521,278	400,378
Total current assets	15,979,792	14,761,209
Other assets		
Cash investments	31,592,051	25,904,234
Nonregulated investments	237,302	182,326
Investment in affiliated companies	44,580,674	43,451,088
Deferred charges	21,546	32,435
Total other assets	76,431,573	69,570,083
Telephone plant, at cost (substantially all pledged as collateral on long-term debt to RUS)		
Telephone plant in service	94,458,031	88,417,852
Telephone plant under construction	11,010,122	14,461,106
Nonoperating plant-land	52,008	52,008
Total	105,520,161	102,930,966
Less accumulated depreciation	(59,988,243)	(59,098,195)
Telephone plant, net	45,531,918	43,832,771
	\$ 137,943,283	\$ 128,164,063

The accompanying notes are an integral
part of the financial statements.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
BALANCE SHEETS
December 31, 2014 and 2013

LIABILITIES AND MEMBERS' EQUITIES

	<u>2014</u>	<u>2013</u>
Current liabilities:		
Current portion of long-term debt	\$ 122,756	\$ 184,125
Accounts payable, includes construction contracts payable of \$192,6176 in 2014 and \$142,506 in 2013	991,903	1,039,612
Customer deposits	9,400	12,050
Accrued expenses	<u>2,592,181</u>	<u>2,168,597</u>
Total current liabilities	<u>3,716,240</u>	<u>3,404,384</u>
Deferred income taxes	<u>10,799,661</u>	<u>9,059,996</u>
Total long term liabilities	10,799,661	9,059,996
Other liabilities and deferred credits:		
Post retirement benefit obligation	-	61,730
Deferred credit	<u>145,346</u>	<u>195,491</u>
Total other liabilities and deferred credits	<u>145,346</u>	<u>257,221</u>
Members' equities:		
Patronage capital	49,304,472	48,354,832
Other equities	73,620,240	68,592,015
Accumulated other comprehensive income (loss)	(988,511)	(2,748,694)
Other member capital	<u>1,345,835</u>	<u>1,244,309</u>
Total members' equities	<u>123,282,036</u>	<u>115,442,462</u>
	<u>\$ 137,943,283</u>	<u>\$ 128,164,063</u>

The accompanying notes are an integral
part of the financial statements.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
STATEMENTS OF INCOME
For The Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Operating revenues:		
Local network services	\$ 8,900,465	\$ 8,455,289
Network access services	9,884,046	9,834,642
Carrier billing and collection	104,782	110,081
Miscellaneous operating revenue	1,819,416	1,765,272
Uncollectible revenue	<u>(118,944)</u>	<u>(109,354)</u>
Total operating revenues	<u>20,589,765</u>	<u>20,055,930</u>
 Operating expenses:		
Plant specific operations	8,403,420	8,086,799
Plant nonspecific operations	1,731,126	1,648,505
Depreciation	6,433,387	5,526,422
Customer operations	1,479,959	1,575,845
Corporate operations	<u>2,632,033</u>	<u>2,480,437</u>
Total operating expenses	<u>20,679,925</u>	<u>19,318,008</u>
 Nonregulated Income	<u>1,155,471</u>	<u>1,131,334</u>
 Operating income	<u>1,065,311</u>	<u>1,869,256</u>
 Nonoperating income	8,630,807	10,312,005
Provision for income taxes	<u>(2,854,599)</u>	<u>(3,726,390)</u>
Nonoperating income net of taxes	<u>5,776,208</u>	<u>6,585,615</u>
 Income before interest	6,841,519	8,454,871
 Interest on long-term debt to RUS, net of interest capitalized \$62,898 in 2014 and \$108,424 in 2013	<u>(81,284)</u>	<u>(264,848)</u>
 Net Income	<u>\$ 6,760,235</u>	<u>\$ 8,190,023</u>

The accompanying notes are an integral
part of the financial statements.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
STATEMENTS OF COMPREHENSIVE INCOME
For The Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Net Income	\$ 6,760,235	\$ 8,190,023
Other comprehensive income		
Postretirement benefit other than pension:		
Unrecognized gain (loss) on assets	1,458,295	(493,669)
Change in unrealized gain (loss) on marketable securities	<u>301,888</u>	<u>533,276</u>
Total comprehensive income	<u>\$ 8,520,418</u>	<u>\$ 8,229,630</u>

The accompanying notes are an integral
part of the financial statements.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
STATEMENTS OF PATRONAGE CAPITAL AND OTHER EQUITIES
For The Years Ended December 31, 2014 and 2013

	Patronage Capital			Accumulated Comprehensive Income	Other Equities
	Assignable	Assigned	Balance		
Balances, January 1, 2013	\$ 9,118,587	\$ 39,749,112	\$ 48,867,699	\$ (2,788,301)	\$ 60,674,833
Patronage capital assigned for the year ended December 31, 2013	(2,446,547)	2,446,547	-	-	-
Refund of overcollected Federal Excise tax for prior year	-	7,583	7,583	-	-
Adjustment for prior refunds	-	(648)	(648)	-	-
Transfer nonoperating margins for 2013	(7,917,211)	-	(7,917,211)	-	7,917,182
Postretirement benefit other than pension Unrecognized loss on assets	-	-	-	(493,669)	-
Net income for the year ended December 31, 2013	8,190,023	-	8,190,023	-	-
Other comprehensive income	-	-	-	533,276	-
Distribution of patronage capital	-	(792,614)	(792,614)	-	-
Balances, December 31, 2013	<u>6,944,852</u>	<u>41,409,980</u>	<u>48,354,832</u>	<u>(2,748,694)</u>	<u>68,592,015</u>
Patronage capital assigned for the year ended December 31, 2014	(3,161,828)	3,161,828	-	-	-
Refund of overcollected Federal Excise tax for prior year	-	8,441	8,441	-	-
Adjustment for prior refunds	-	73	73	-	-
Transfer nonoperating margins for 2014	(5,028,195)	-	(5,028,195)	-	5,028,225
Postretirement benefit other than pension Unrecognized loss on assets	-	-	-	1,458,295	-
Net income for the year ended December 31, 2014	6,760,235	-	6,760,235	-	-
Other comprehensive income	-	-	-	301,888	-
Distribution of patronage capital	-	(790,914)	(790,914)	-	-
Balances, December 31, 2014	<u>\$ 5,515,064</u>	<u>\$ 43,789,408</u>	<u>\$ 49,304,472</u>	<u>\$ (988,511)</u>	<u>\$ 73,620,240</u>

The accompanying notes are an integral
part of the financial statements.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
STATEMENTS OF CASH FLOWS
For The Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Cash flows from operating activities:		
Net income	\$ 6,760,235	\$ 8,190,023
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,433,387	5,526,422
Income from investment in affiliated companies	(7,790,137)	(9,717,402)
Refund of Federal Excise taxes	8,441	7,583
Changes in operating assets and liabilities:		
Decrease (increase) in accounts receivable	399,749	623,024
Decrease (increase) in inventory	8,439	(17,324)
Decrease (increase) in prepaid expenses	(120,900)	(11,986)
(Decrease) increase in accounts payable	(508,178)	(201,492)
(Decrease) increase in customer deposits	(2,650)	(2,350)
(Decrease) increase in deferred taxes	1,736,665	(2,988,317)
(Decrease) increase in accrued expenses	<u>423,584</u>	<u>276,919</u>
Net cash provided by operating activities	<u>7,348,635</u>	<u>1,685,100</u>
Cash flows from investing activities:		
Purchases of property, plant and equipment	(6,547,347)	(7,820,138)
Plant removal costs	(126,790)	(15,963)
Decrease (increase) in nonregulated investments	(54,976)	32,003
Investment in affiliated companies	8,875,712	5,920,303
Investments - other	(2,215,161)	(431,070)
Purchases of temporary investments	(3,857,356)	(2,945,767)
Maturity of temporary investments	3,569,825	9,441,283
Purchases of cash investments	(10,164,700)	(5,547,979)
Maturity of cash investments	4,080,287	-
Decrease (increase) in deferred charges	<u>10,889</u>	<u>444,559</u>
Net cash used in investing activities	<u>(6,429,617)</u>	<u>(922,769)</u>

The accompanying notes are an integral part of the financial statements.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
STATEMENTS OF CASH FLOWS, CONCLUDED
For The Years Ended December 31, 2014 and 2013

	<u>2014</u>	<u>2013</u>
Cash flows from financing activities:		
Distributions of patronage capital	\$ (790,914)	\$ (792,614)
Principal payments to Rural Utilities Service	(61,369)	(2,497,223)
Principal payments to CoBank	-	(55,781)
(Decrease) increase in deferred credits	(111,875)	30,988
Other member capital	<u>101,526</u>	<u>107,323</u>
Net cash (used) provided by financing activities	<u>(862,632)</u>	<u>(3,207,307)</u>
Net (decrease) increase in cash and cash equivalents	56,386	(2,444,976)
Cash and cash equivalents at beginning of year	<u>3,607,197</u>	<u>6,052,173</u>
Cash and cash equivalents at end of year	<u>\$ 3,663,583</u>	<u>\$ 3,607,197</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest, net of interest capitalized of \$124,584 in 2014 and \$124,584 in 2013	<u>\$ 206,297</u>	<u>\$ 327,747</u>
Income taxes	<u>\$ 984,552</u>	<u>\$ 6,671,981</u>

The accompanying notes are an integral
part of the financial statements.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies:

Principles of Consolidation:

The consolidated financial statements include the accounts of Duo County Telephone Cooperative Corporation, Inc. and its wholly owned subsidiaries, Diversified Holding Corporation and Cumberland Cellular, Inc. All material intercompany transactions have been eliminated.

General:

The Cooperative maintains its accounts in accordance with the Uniform System of Accounts prescribed for telephone companies by the Federal Communications Commission. The financial statements reflect the application of certain accounting policies described in this note.

Nature of Business:

Duo County Telephone Cooperative Corporation, Inc. Cooperative Corporation, Inc., provides telephone service in a four-county area of south central Kentucky. The Cooperative grants credit to customers, substantially all of whom are local residents and commercial businesses.

Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of management estimates and assumptions that affect the reporting amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reporting amounts of the revenues and expenses during the reporting period. Actual results could differ from those estimates.

Telephone Plant:

Telephone plant is stated at original cost, which includes material, labor, transportation and such indirect items as engineering, supervision and employee fringe benefits. As property units are retired in the ordinary course of business, the cost of the property plus removal cost, less salvage, is charged to accumulated depreciation. Listed below are the major classes of telephone plant as of December 31, 2014 and 2013:

	<u>2014</u>	<u>2013</u>	Depreciation <u>Rate</u>
Organization	\$ 14,728	\$ 28,323	0.0%
Land	664,790	664,790	0.0%
Buildings	7,874,242	7,837,617	2.7%
Central Office Equipment	23,874,307	22,725,197	7.5-11.9%
Cable and Wire Facilities	55,202,018	50,375,650	2.2-8.9%
Furniture and Office Equipment	1,393,696	1,386,743	7.5-8.7%
General Purpose Computers	1,005,450	989,318	15.8%
Vehicles	1,227,989	1,249,217	12.1%
Other Work Equipment	666,684	626,870	12.1%
Intangible - CATV	1,529,507	1,529,507	0.0%
Goodwill	1,004,620	1,004,620	0.0%
	<u>\$ 94,458,031</u>	<u>\$ 88,417,852</u>	

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED

1. Summary of Significant Accounting Policies, Continued:

Depreciation:

Depreciation is calculated by the straight-line method designed to amortize the cost of various classes of depreciable assets over their estimated useful lives.

Deregulated Customer Premises Equipment:

Deregulated CPE is stated at cost. The Cooperative provides for depreciation on a straight-line basis at an annual rate of depreciation which will amortize the cost of the equipment over its estimated useful life.

Cash and Cash Equivalents:

For purposes of the statement of cash flows, the Cooperative considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

Nonregulated Investments:

This balance reflects the Cooperative's permanent net investment in deregulated CPE and internet equipment. Following is a summary of net income from deregulated operations for the years ended December 31, 2014 and 2013:

	<u>2014</u>	<u>2013</u>
Income from operations	\$ 3,978,592	\$ 3,915,068
Expenses	<u>(2,823,121)</u>	<u>(2,783,734)</u>
Net income	<u>\$ 1,155,471</u>	<u>\$ 1,131,334</u>

Investment in Affiliated Companies:

This balance represents the Cooperative's investments in affiliates for the purpose of providing cellular telephone services. Duo County Telephone Cooperative Corporation, Inc. owns 20% of Bluegrass Network, LLC. Cumberland Cellular, Inc. owns 20% of Bluegrass Telcom and 62.5% of Cumberland Cellular Partnership. The investments are accounted for using the equity method. Additionally, the Cooperative's 20% investment in a partnership is accounted for using the equity method.

In March 2003, the Cooperative's affiliate Cumberland Cellular, Inc., purchased the assets of a cable television system in Russell County, Kentucky. The operations of the cable system are reflected in the financial statements of Cumberland Cellular, Inc. for 2014 and 2013.

In July 2006, the Cooperative's affiliate Cumberland Cellular, Inc. purchased the assets of a cable television system in Columbia-Adair County, Kentucky. The operations of the cable system are reflected in the financial statements of Cumberland Cellular, Inc. for 2014 and 2013.

Other Member Capital:

This balance represents unclaimed distributions of patronage capital. After a statutory waiting period, these balances will be re-assigned to the Cooperative's existing patrons.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED

1. Summary of Significant Accounting Policies, Continued:

Postretirement Benefit Plans:

The Corporation sponsors a defined benefit plan that provides medical and life insurance coverage to retirees and their dependents. Through 2004 the participating retirees and dependents contributed 0% of the project cost of coverage. For employees hired after July 1, 2005 the Company contributed 100% until spouse and retiree were 65. For employees hired after December 1, 2012, the Company pays no health insurance for retirees.

The following sets forth the accumulated post-retirement benefit obligation, the change in plan assets, and the component of accrued post-retirement benefit cost and net periodic benefit cost as of December 31, 2014 and 2013.

	<u>2014</u>	<u>2013</u>
Accumulated post-retirement benefit obligation, beginning	\$ 9,081,581	\$ 7,562,433
Service cost	218,636	225,046
Interest cost	394,411	401,777
Plan Participants contributions	(263,078)	(270,630)
Actuarial loss	(1,458,295)	670,685
Benefits paid	<u>936,775</u>	<u>492,270</u>
Accumulated post retirement benefit obligation, ending	<u>\$ 8,910,030</u>	<u>\$ 9,081,581</u>
Fair value of plan assets - beginning of year	\$ 9,019,851	\$ 7,994,372
Employer contributions	(263,078)	(270,630)
Plan Participants contributions	-	-
Unrealized gains on assets	2,697,533	1,788,379
Benefits paid	<u>(936,774)</u>	<u>(492,270)</u>
Fair value of plan assets - end of year	<u>10,517,532</u>	<u>9,019,851</u>
Unfunded status	\$ (1,607,502)	\$ (61,730)
Unrecognized net actuarial loss	<u>1,839,742</u>	<u>3,298,036</u>
Net amount recognized	<u>\$ 3,447,244</u>	<u>\$ 3,236,306</u>
Unfunded status	\$ (1,607,502)	\$ 61,730
Current liabilities	-	309,801
Noncurrent liabilities	<u>(1,607,502)</u>	<u>(248,071)</u>
Service cost	\$ 218,636	\$ 225,046
Interest cost	394,411	401,777
Amortization of net actuarial gain	57,910	144,421
Expected return on assets	<u>(764,065)</u>	<u>(655,276)</u>
Net periodic benefit cost	<u>\$ (93,108)</u>	<u>\$ 115,968</u>
Net amount recognized (included in other comprehensive income)	<u>\$ 1,458,295</u>	<u>\$ (493,669)</u>
Amounts in other comprehensive income expected to be realized in the subsequent year - actuarial gain	<u>\$ 57,910</u>	<u>\$ 144,421</u>

The discount rate used in determining the accumulated postretirement benefit obligation was 4.5% and 4.5% for the years ending December 31, 2014 and 2013, respectively

Expected benefit payments from the plan for the year ending December 31, 2014 total \$293,915.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED

1. Summary of Significant Accounting Policies, Continued:

For measurement purposes, an 8% annual rate increase in the per capita cost of covered health care benefits was used for the year ended December 31, 2014. The anticipated future rates are as follows:

2015	6.00%
2016	5.50%
2017	5.00%
2018	5.00%
2019	5.00%
2020-2023	5.00%

An additional 1% increase in the trend utilized for measurement purposes in 2014 would have resulted in an increase in the accumulated postretirement benefit obligation of approximately 1.5 million.

Subsequent Events:

Management has evaluated subsequent events through March 26, 2015, the date which the financial statements were available to be issued.

Reclassifications:

Certain amounts in the prior year financial statements have been reclassified for comparative purposes to conform with the presentation in the current year financial statements.

Related Party Transactions:

Related party transactions have been eliminated during the consolidation of the financial statements for the years ended December 31, 2014 and 2013.

2. Mortgage Notes:

Long-term debt is represented by mortgage notes payable to the United States of America. Principal and interest payments are due in both monthly and quarterly installments. It is estimated that installments of \$122,756 are payable within the next twelve months to the United States of America. The notes are scheduled to be repaid at various times from May 2009 to April 2023. At December 31, 2014, the Cooperative has unadvanced loan funds in amount of \$8,734,713.

As of December 31, 2014, the Cooperative has made advanced payments in the amount of \$3,466,119 on its mortgage notes payable to the United States of America.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED

2. Mortgage Notes, Concluded:

Following is a summary of outstanding long-term debt:

	<u>2014</u>	<u>2013</u>
Due to United States of America:		
5% First Mortgage Notes	\$ 861,990	\$ 1,107,942
4.8375% First Mortgage Notes	-	15,819
3.56% - 5.05% First Mortgage Notes	<u>3,053,598</u>	<u>6,136,529</u>
Total due to the United States of America	<u>3,915,588</u>	<u>7,260,290</u>
Less unadvanced loans	(326,713)	(326,713)
Less RUS advanced payments	(3,466,119)	(6,749,452)
Less current maturities	<u>(122,756)</u>	<u>(184,125)</u>
	<u>\$ -</u>	<u>\$ -</u>

The maturities of long-term debt for each of the five years succeeding the balance sheet date are as follows:

2014	\$122,756
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Due to the amount of RUS advanced payments, the balance of long-term debt is shown as current.

The long-term debt agreements and the bylaws of the Cooperative contain restrictions on the return to patrons of capital credits. These restrictions require the maintenance of defined amounts of members' equity and working capital.

3. Cash and Cash Equivalents:

All deposits are in various financial institutions and are carried at cost.

	<u>2014</u>		<u>2013</u>	
	<u>Carrying Amount</u>	<u>Bank Balance</u>	<u>Carrying Amount</u>	<u>Bank Balance</u>
Insured (FDIC)	\$ 1,008,180	\$ 848,483	\$ 1,019,410	\$ 858,633
Uninsured				
Collateral held by pledging bank's trust department in Cooperative's name	<u>2,655,403</u>	<u>2,147,651</u>	<u>2,587,787</u>	<u>3,048,162</u>
Total deposit	<u>\$ 3,663,583</u>	<u>\$ 2,996,134</u>	<u>\$ 3,607,197</u>	<u>\$ 3,906,795</u>

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED

4. Investments:

Marketable securities have been classified as available-for-sale according to management's intent. Realized gains and losses on all marketable securities are determined by specific identification and are charged or credited to earnings.

Cost and fair value of the company's available-for-sale securities at December 31, 2014 and 2013 have been segregated as follows:

<u>December 31, 2014</u>			
	<u>Cost</u>	<u>Market</u>	<u>Unrealized Gain/(Loss)</u>
Cash Equivalents	\$ 66,118	\$ 66,118	\$ -
Equity Securities	<u>3,141,192</u>	<u>3,443,080</u>	<u>301,888</u>
Total Available-For-Sale	<u>\$ 3,207,310</u>	<u>\$ 3,509,198</u>	<u>\$ 301,888</u>

<u>December 31, 2013</u>			
	<u>Cost</u>	<u>Market</u>	<u>Unrealized Gain/(Loss)</u>
Cash Equivalents	\$ 63,539	\$ 63,539	\$ -
Equity Securities	<u>2,515,787</u>	<u>3,049,063</u>	<u>533,276</u>
Total Available-For-Sale	<u>\$ 2,579,326</u>	<u>\$ 3,112,602</u>	<u>\$ 533,276</u>

Available-for-sale securities are carried in the financial statements at fair market value and included in other investments on the financial statements. Net unrealized holding gains and losses in the amount of \$301,888 have been included in accumulated other comprehensive income for the year ended December 31, 2014 and \$533,276 for December 31, 2013.

5. Temporary Cash Investments:

In 1996, the Cooperative adopted Financial Accounting Standards No. 115, "Accounting for Certain Investments in Debt and Equity Securities". This statement addresses the accounting and reporting for investments in equity securities that have readily determinable fair values and for all investments in debt securities.

All debt securities of the Cooperative are considered to be held to maturity. The carrying amounts and approximate market value of held to maturity investments are:

	<u>Amortized Cost</u>	<u>Net Unrealized Gains(Losses)</u>	<u>Market Value</u>
U.S. Treasury Securities - 2014	\$ 40,076,340	\$ 988,648	\$ 41,064,988
U.S. Treasury Securities - 2013	\$ 33,118,930	\$ 467,176	\$ 33,586,106

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, CONTINUED

5. Temporary Cash Investments, Concluded:

The maturities of held to maturity investments and their approximate market value at December 31, 2014 and 2013, were as follows:

	<u>2014</u>		<u>2013</u>	
	<u>Amortized Cost</u>	<u>Market Value</u>	<u>Amortized Cost</u>	<u>Market Value</u>
Due in one year or less (included in cash and temporary cash investments)	\$ 8,484,295	\$ 9,499,962	\$ 7,214,686	\$ 7,189,061
Due after one year	<u>31,592,051</u>	<u>31,565,026</u>	<u>25,904,234</u>	<u>26,397,045</u>
	<u>\$ 40,076,346</u>	<u>\$ 41,064,988</u>	<u>\$ 33,118,920</u>	<u>\$ 33,586,106</u>

6. Provision for Income Taxes:

The Corporation has been exempt from federal income taxes as a cooperative telephone company under Section 501(c)(12) of the Internal Revenue Code. In 1991, the Internal Revenue Service issued a Technical Advice Memorandum, which interprets certain types of revenues to be excluded in determining when the Cooperative satisfies the 85 percent income test to qualify for tax exempt status. By applying these interpretations, the Cooperative does not qualify in the current year for the tax exempt status. The Company's provision for income taxes differs from applying the statutory U.S. federal income tax rate to income before income taxes. The primary differences result from providing for state income taxes and from deducting certain expenses for financial statement purposes but not for federal tax purposes.

The provision for income taxes for 2014 and 2013 consists of the following:

	<u>2014</u>	<u>2013</u>
Current income tax expense	\$ 1,114,934	\$ 5,396,215
Deferred income taxes	<u>1,739,665</u>	<u>(1,669,825)</u>
Provision for income taxes	<u>\$ 2,854,599</u>	<u>\$ 3,726,390</u>

A cumulative net deferred tax liability is included in other liabilities. The components of the liability are as follows:

	<u>2014</u>	<u>2013</u>
Differences in Depreciation Methods	<u>\$ 10,799,661</u>	<u>\$ 9,059,996</u>

The Cooperative follows the recognition requirements for uncertain income tax positions as required by generally accepted accounting principles. The Company has no tax position at December 31, 2014 for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of such deductibility. The Cooperative's policy is to classify income tax related interest and penalties in interest expense and other expenses, respectively. No such interest or penalties were recognized during the periods presented.

The Company files income tax returns in the U.S. federal jurisdiction, and various state and local jurisdictions. The Company is no longer subject to U.S. federal, state and local income tax examinations by tax authorities for years before 2011.

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS, CONCLUDED

7. Deferred Charges:

Following is a summary of amounts recorded as deferred charges approved by RUS per 1773.33(h) as of December 31, 2014 and 2013 which have been approved in writing by RUS:

Deferred Debits:	<u>2014</u>	<u>2013</u>
Information Systems	\$ 21,546	\$ 32,435
	<u>\$ 21,546</u>	<u>\$ 32,435</u>
 Deferred Credits:		
Other Deferred Taxes	\$ 145,346	\$ 195,491

8. Pension Plan:

The Cooperative has a non-contributory defined benefit pension plan covering substantially all of its employees. Effective July 1, 1984, the Cooperative changed from its original plan to one sponsored by the National Telephone Cooperative Association.

At the time of transfer to the new Plan, the Cooperative funded all past service costs. Contributions to this Plan for the years ended December 31, 2014 and 2013 were \$558,049 and \$490,656. The fund covers all vested benefits under the Plan. The Plan has been approved by the Internal Revenue Service. As the Cooperative is only one of several employers participating in the Plan, it is not practicable to determine if the vested benefits of the Cooperative's employees exceed the Cooperative's portion of the Plan assets.

The accumulated plan benefit information using the latest actuarial information applicable for each plan year is as follows:

	<u>January 1, 2014</u>	<u>January 1, 2013</u>
Accumulated benefit obligation	\$(1,855,866,101)	\$(2,055,959,200)
Plan assets at fair value	<u>1,592,981,168</u>	<u>1,450,738,554</u>
 Funded Status	 <u>\$ (262,884,933)</u>	 <u>\$ (605,220,646)</u>

Additionally, the Cooperative has a 401 (K) Plan. The terms of the Plan call for an elective contribution from employees of 1% or more of their salaries while the Cooperative contributes 1% of their salary. Total pension expenses related to the Plan for 2014 and 2013 were \$31,351 and \$30,862.

ADDITIONAL INFORMATION



CAMPBELL, MYERS AND RUTLEDGE, PLLC

Cindy L. Greer, CPA ▪ L. Joe Rutledge, CPA ▪ Jonathan W. Belcher, CPA ▪ R. Brent Billingsley, CPA

Skip R. Campbell, CPA ▪ Sammie D. Parsley, CPA ▪ Ryan Mosier, CPA ▪ Jenna B. Pace, CPA

Independent Auditors' Report
on Consolidating Information

Board of Directors
Duo County Telephone Cooperative Corporation, Inc.
Jamestown, Kentucky 42629

We have audited the consolidated financial statements of Duo County Telephone Cooperative Corporation, Inc. and Subsidiaries as of and for the years ended December 31, 2014 and 2013, and our report thereon dated March 26, 2015, which expressed an unmodified opinion on those financial statements, appears on pages one and two. Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information presented in Schedule I and II and III is presented for purposes of additional analysis of the consolidated financial statements rather than to present the financial position, results of operations, and cash flows of the individual companies, and it is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The consolidating information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the consolidating information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Campbell, Myers & Rutledge, PLLC

Certified Public Accountants

March 26, 2015

**DUO COUNTY TELEPHONE COOPERATIVE CORPORATION INC.
SCHEDULE I – CONSOLIDATING BALANCE SHEET**

December 31, 2014

	Duo County Telephone Cooperative Corp., Inc.	Diversified Holding Corporation	Cumberland Cellular, Inc.	Consolidating Entries	Consolidated Totals
ASSETS					
Cash and equivalents	\$ 1,924,172	\$ 136,953	\$ 1,602,255	\$ -	\$ 3,663,380
Temporary cash investments	1,185,000	-	3,175,290	-	4,360,290
Cash, RUS construction fund	203	-	-	-	203
Marketable securities	-	-	3,509,198	-	3,509,198
Accounts receivable	1,119,807	-	991,473	(1)(577,094)	1,534,186
Material and supplies - Regulated	1,210,048	-	981,206	-	2,191,254
Accrued interest receivable	55,086	-	144,917	-	200,003
Prepayments	521,278	-	-	-	521,278
Total current assets	<u>6,015,594</u>	<u>136,953</u>	<u>10,404,339</u>	<u>(577,094)</u>	<u>15,979,792</u>
Other assets					
Cash investments	9,394,407	-	22,197,644	-	31,592,051
Investments in affiliated company	68,305,200	68,175,467	38,203,811	(2,680,000) (2)	38,203,811
				(133,800,667) (3)	
Other investments	6,336,579	-	40,284	-	6,376,863
Nonregulated investments	237,302	-	-	-	237,302
Deferred charges	21,546	-	-	-	21,546
Total other assets	<u>84,295,034</u>	<u>68,175,467</u>	<u>60,441,739</u>	<u>(136,480,667)</u>	<u>76,431,573</u>
Telephone plant in service	74,073,836	-	20,384,195	-	94,458,031
Telephone plant under construction	10,865,144	-	196,986	-	11,062,130
Total telephone plant	<u>84,938,980</u>	<u>-</u>	<u>20,581,181</u>	<u>-</u>	<u>105,520,161</u>
Depreciation reserve	<u>49,090,377</u>	<u>-</u>	<u>10,897,866</u>	<u>-</u>	<u>59,988,243</u>
Total telephone plant less reserve	<u>35,848,603</u>	<u>-</u>	<u>9,683,315</u>	<u>-</u>	<u>45,531,918</u>
Total assets	<u>\$ 126,159,231</u>	<u>\$ 68,312,420</u>	<u>\$ 80,529,393</u>	<u>\$ (137,057,761)</u>	<u>\$ 137,943,283</u>
LIABILITIES AND EQUITY					
Accounts payable	\$ 1,273,810	\$ 4,704	\$ 290,483	(577,094) (1)	\$ 991,903
Customer deposits	9,400	-	-	-	9,400
Accrued liabilities	2,177,113	2,516	412,552	-	2,592,181
Current portion of long-term debt	122,756	-	-	-	122,756
Total current liabilities	<u>3,583,079</u>	<u>7,220</u>	<u>703,035</u>	<u>(577,094)</u>	<u>3,716,240</u>
Deferred income taxes-noncurrent	-	-	10,799,661	-	10,799,661
Total long-term liabilities	<u>-</u>	<u>-</u>	<u>10,799,661</u>	<u>-</u>	<u>10,799,661</u>
Other deferred credits	145,346	-	-	-	145,346
Total other liabilities and deferred credits	<u>145,346</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>145,346</u>
Capital stock	-	1,400,000	1,280,000	(2,680,000) (2)	-
Patronage capital credits	50,762,767	-	-	-	50,762,767
Total retained margins	73,620,240	66,905,200	66,895,467	(133,800,667) (3)	73,620,240
Accumulated other comprehensive income(loss)	(3,298,036)	-	851,230	-	(2,446,806)
Other equities	1,345,835	-	-	-	1,345,835
Retained margins and capital credits	<u>122,430,806</u>	<u>68,305,200</u>	<u>69,026,697</u>	<u>(136,480,667)</u>	<u>123,282,036</u>
Total liabilities and equity	<u>\$ 126,159,231</u>	<u>\$ 68,312,420</u>	<u>\$ 80,529,393</u>	<u>\$ (137,057,761)</u>	<u>\$ 137,943,283</u>

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
SCHEDULE II CONSOLIDATING STATEMENT OF INCOME AND COMPREHENSIVE INCOME
For the Year Ended December 31, 2014

	Duo County Telephone Cooperative Corp., Inc.	Diversified Holding Corporation	Cumberland Cellular, Inc.	Consolidating Entries	Consolidated Totals
Local network services revenue	\$ 2,600,609	\$ -	\$ 6,299,856	\$ -	\$ 8,900,465
Network access service revenue	9,884,046	-	-	-	9,884,046
Carrier billing and collection revenue	104,782	-	-	-	104,782
Miscellaneous revenues	1,350,448	-	468,968	-	1,819,416
Less: Uncollectible revenues	<u>(22,121)</u>	<u>-</u>	<u>(96,823)</u>	<u>-</u>	<u>(118,944)</u>
Total operating revenues	<u>13,917,764</u>	<u>-</u>	<u>6,672,001</u>	<u>-</u>	<u>20,589,765</u>
Plant specific operating expenses	3,837,764	-	4,565,656	-	8,403,420
Plant nonspecific operating expenses	1,731,126	-	-	-	1,731,126
Depreciation and amortization expense	4,702,255	-	1,731,132	-	6,433,387
Customer operations expense	1,323,662	-	156,297	-	1,479,959
Corporate operations expense	<u>1,704,202</u>	<u>1,785</u>	<u>926,046</u>	<u>-</u>	<u>2,632,033</u>
Total operating expenses	<u>13,299,009</u>	<u>1,785</u>	<u>7,379,131</u>	<u>-</u>	<u>20,679,925</u>
Nonregulated income	<u>1,155,471</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,155,471</u>
Telephone operating income (loss)	<u>1,774,226</u>	<u>(1,785)</u>	<u>(707,130)</u>	<u>-</u>	<u>1,065,311</u>
Nonoperating income	5,112,293	3,878,924	7,394,890	(3,876,399) (1) (3,878,901) (1)	8,630,807
Provision from income taxes	<u>45,000</u>	<u>740</u>	<u>2,808,859</u>	<u>-</u>	<u>2,854,599</u>
Nonoperating income net of taxes	<u>5,067,293</u>	<u>3,878,184</u>	<u>4,586,031</u>	<u>(7,755,300)</u>	<u>5,726,208</u>
Income before interest	6,841,519	3,876,399	3,878,901	(7,755,300)	6,841,519
Interest on funded debt, net	<u>(81,284)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(81,284)</u>
Net income	6,760,235	3,876,399	3,878,901	(7,755,300)	6,760,235
Other comprehensive income and post retirement benefits	<u>1,458,294</u>	<u>-</u>	<u>301,888</u>	<u>-</u>	<u>1,760,183</u>
Total comprehensive income	<u>\$ 8,218,529</u>	<u>\$ 3,876,399</u>	<u>\$ 4,180,789</u>	<u>\$ (7,755,300)</u>	<u>\$ 8,520,418</u>

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
SCHEDULE III CONSOLIDATING STATEMENT OF CASH FLOWS
For the Year Ended December 31, 2014

	Duo County Telephone Cooperative Corp., Inc.	Diversified Holding Corporation	Cumberland Cellular, Inc.	Consolidating Entries	Consolidated Totals
Cash flows from operating activities:					
Net income	\$ 6,760,235	\$ 3,876,399	\$ 3,878,901	\$ (7,755,300)	\$ 6,760,235
Adjustments to reconcile net income to net cash provided by operating activities:					
Depreciation and amortization	4,702,255	-	1,731,132	-	6,433,387
Income from investment in affiliated companies	(4,565,659)	(3,878,901)	(7,100,877)	7,755,300	(7,790,137)
Refund of Federal Excise taxes	8,441	-	-	-	8,441
Changes in operating assets and liabilities:					
Decrease (increase) in accounts receivable	83,143	-	(194,136)	510,742	399,749
Decrease (increase) in inventory	(93,513)	-	101,952	-	8,439
Decrease (increase) in prepaid expenses	(120,900)	-	-	-	(120,900)
(Decrease) increase in accounts payable	(3,536)	580	5,520	(510,742)	(508,178)
(Decrease) increase in customer deposits	(2,650)	-	-	-	(2,650)
(Decrease) increase in deferred taxes	-	-	1,736,665	-	1,736,665
(Decrease) increase in accrued expenses	260,939	-	162,645	-	423,584
Net cash provided by operating activities	<u>7,028,755</u>	<u>(1,922)</u>	<u>321,802</u>	<u>-</u>	<u>7,348,635</u>
Cash flows from investing activities:					
Purchases of property, plant and equipment	(5,796,249)	-	(751,098)	-	(6,547,347)
Plant removal costs	(126,790)	-	-	-	(126,790)
Decrease (increase) in nonregulated investments	(54,976)	-	-	-	(54,976)
Investment in affiliated companies	689,260	-	8,186,452	-	8,875,712
Investments - other	(2,215,161)	-	-	-	(2,215,161)
Purchases of temporary investments	(950,000)	-	(2,907,356)	-	(3,857,356)
Maturity of temporary investments	1,765,767	-	1,804,058	-	3,569,825
Purchases of cash investments	(3,998,046)	-	(6,166,654)	-	(10,164,700)
Maturity of cash investments	4,080,287	-	-	-	4,080,287
Decrease (increase) in deferred charges	10,889	-	-	-	10,889
Net cash used in investing activities	<u>(6,595,019)</u>	<u>-</u>	<u>165,402</u>	<u>-</u>	<u>(6,429,617)</u>

DUO COUNTY TELEPHONE COOPERATIVE CORPORATION, INC.
SCHEDULE III CONSOLIDATING STATEMENT OF CASH FLOWS CONCLUDED
For the Year Ended December 31, 2014

	Duo County Telephone Cooperative Corp., Inc.	Diversified Holding Corporation	Cumberland Cellular, Inc.	Consolidating Entries	Consolidated Totals
Cash flows from financing activities:					
Capital stock called	\$ -	\$ -	\$ -	\$ -	\$ -
Distributions of patronage capital	(790,914)	-	-	-	(790,914)
Principal payments to Rural Utilities Service	(61,369)	-	-	-	(61,369)
Principal payments to CoBank	-	-	-	-	-
(Decrease) increase in deferred credits	(111,875)	-	-	-	(111,875)
Other member capital	101,526	-	-	-	101,526
Net cash (used) provided by financing activities	<u>(862,632)</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(862,632)</u>
Net (decrease) increase in cash and cash equivalents	(428,896)	(1,922)	487,204	-	56,386
Cash and cash equivalents at beginning of year	<u>2,353,271</u>	<u>138,875</u>	<u>1,115,051</u>	<u>-</u>	<u>3,607,197</u>
Cash and cash equivalents at end of year (Notes 1 and 4)	<u>\$ 1,924,375</u>	<u>\$ 136,953</u>	<u>\$ 1,602,255</u>	<u>\$ -</u>	<u>\$ 3,663,583</u>
Supplemental disclosures of cash flow information:					
Cash paid during the year for:					
Interest, net of interest capitalized of \$124,584 in 2014 and \$62,898 in 2013	<u>\$ 206,297</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 206,297</u>
Income taxes	<u>\$ 68,401</u>	<u>\$ 175</u>	<u>\$ 915,976</u>	<u>\$ -</u>	<u>\$ 984,552</u>



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INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER MATTERS
BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Board of Directors
Duo County Telephone Cooperative Corporation, Inc.
Jamestown, Kentucky 42629

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of Duo County Telephone Cooperative Corporation, Inc. as of and for the years ended December 31, 2014 and 2013, and the related statements of operations, comprehensive income, patronage capital and other equities and cash flows for the years then ended, and the related notes to the consolidated financial statements, which collectively comprise Duo County Telephone Cooperative Corporation, Inc.'s basic financial statements, and have issued our report thereon dated March 26, 2015.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered Duo County Telephone Cooperative Corporation, Inc.'s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Duo County Telephone Cooperative Corporation, Inc.'s internal control. Accordingly, we do not express an opinion on the effectiveness of Duo County Telephone Cooperative Corporation, Inc.'s internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Duo County Telephone Cooperative Corporation, Inc.'s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Campbell, Myers & Rutledge, PLLC

Certified Public Accountants

March 26, 2015



CAMPBELL, MYERS AND RUTLEDGE, PLLC

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH ASPECTS
OF CONTRACTUAL AGREEMENTS AND REGULATORY REQUIREMENTS
FOR TELECOMMUNICATION BORROWERS

Board of Directors
Duo County Telephone
Cooperative Corporation
Jamestown, Kentucky 42629

Independent Auditor's Report

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the consolidated financial statements of Duo County Telephone Cooperative Corporation and Subsidiaries, which comprise the balance sheet as of December 31, 2014 and 2013, and the related statements of income, comprehensive income and patronage capital and other equities, changes in cash flows for the year ended, and the related notes to the financial statements, and have issued our report thereon dated March 26, 2015. In accordance with *Government Auditing Standards*, we have also issued our report dated March 26, 2015, on our consideration of Duo County Telephone Cooperative Corporation, Inc.'s internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. No reports other than the reports referred to above have been furnished to management.

In connection with our audit, nothing came to our attention that caused us to believe that Duo County Telephone Cooperative Corporation, Inc. failed to comply with the terms, covenants, provisions, or conditions of their loan, grant, and security instruments as set forth in 7 CFR Part 1773, Policy on Audits of Rural Utilities Service Borrowers, & 1773.33 clarified in the RUS policy memorandum dated March 26, 2014, insofar as they relate to accounting matters as enumerated below. However, our audit was not directed primarily toward obtaining knowledge of noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding Duo County Telephone Cooperative Corporation, Inc.'s noncompliance with the above-referenced terms, covenants, provisions, or conditions of the contractual agreements and regulatory requirements, insofar as they relate to accounting matters. In connection with our audit, we noted no matters regarding Duo County Telephone Cooperative Corporation, Inc.'s accounting and records to indicate that Duo County Telephone Cooperative Corporation, Inc. did not:

Maintain adequate and effective accounting procedures;

Utilize adequate and fair methods for accumulating and recording labor, material, and overhead costs, and the distribution of these costs to construction, retirement, and maintenance or other expense accounts;

Reconcile continuing property records to the controlling general ledger plant accounts;

Clear construction accounts and accrue depreciation on completed construction;

Record and properly price the retirement of plant;

Seek approval of the sale, lease or transfer of capital assets and disposition of proceeds for the sale or lease of plant, material, or scrap;

Maintain adequate control over materials and supplies;

Prepare accurate and timely Financial and Operating Reports;

Obtain RUS approval to enter into any contract for the management, operation, or maintenance of the borrower's system if the contract covers all or substantially all of the telecommunication system;

Disclose material related party transactions in the financial statements, in accordance with requirements for related parties in generally accepted accounting principles;

Record depreciation in accordance with RUS requirements (See RUS Bulletin 183-1, Depreciation Rates and Procedures);

Comply with the requirements for the detailed schedule of deferred debits and deferred credits; and

Comply with the requirements for the detailed schedule of investments. A detailed schedule of investments is as follows:

Diversified Holding is a wholly owned subsidiary which invests in businesses providing cellular telephone service and cable television service. The Cooperative accounts for the investment on the equity basis.

Bluegrass Network LLC represents the Cooperative's 20% investment in a partnership which provides cellular telephone service. The Cooperative accounts for the investment on the equity basis.

Investment in Subsidiary Company:
 Original Investment Cost - 1997 \$ -

Investment Advances:

	<u>Diversified Holding Corp.</u>	<u>Bluegrass Network LLC</u>
12/31/90	\$ 3,400,000	\$ -
12/31/91	1,100,000	-
12/31/92	130,000	-
12/31/93	300,000	-
12/31/94	540,000	5,000
12/31/95	160,000	341,000
12/31/96	-	400,000
12/31/97	-	190,000
12/31/98	-	-
12/31/99	-	-
12/31/00	-	-
12/31/01	-	-
12/31/02	-	-
12/31/03	3,000,000	-
12/31/04	770,000	-
12/31/05	-	-
12/31/06	3,000,000	-
12/31/07	1,000,000	-
12/31/08	-	-
12/31/09	-	-
12/31/10	-	-
12/31/11	-	-
12/31/12	(6,000,000)	-
12/31/13	(6,000,000)	-
12/31/14	\$ -	-
Total Contributions	\$ 1,400,000	\$ 936,000

Undistributed (Losses) Earnings:

	<u>Diversified Holding Corp.</u>	<u>Bluegrass Network LLC</u>
12/31/90	\$ 19,208	\$ -
12/31/91	89,940	-
12/31/92	(23,732)	-
12/31/93	14,582	-
12/31/94	122,030	-
12/31/95	469,230	158
12/31/96	600,451	15,389
12/31/97	876,694	32,110
12/31/98	678,663	182,619
12/31/99	844,128	216,047
12/31/00	662,365	193,730
12/31/01	788,508	149,778
12/31/02	984,763	146,181
12/31/03	958,217	141,384
12/31/04	2,055,836	231,989
12/31/05	2,877,511	257,798
12/31/06	4,777,093	248,792
12/31/07	5,683,016	288,504
12/31/08	6,490,036	386,497
12/31/09	6,945,556	424,140
12/31/10	7,336,840	389,346
12/31/11	7,174,008	557,902
12/31/12	7,549,307	654,364
12/31/13	5,054,551	631,435
12/31/14	3,876,399	689,259
Total Undistributed (Losses) Earnings	66,905,200	5,837,422
Original Investment and Investment Advances	1,400,000	936,000
Partnership Distribution as of 12/31/14	-	(2,212,744)
Book Value 12/31/14	\$68,305,200	\$ 4,560,678

This report is intended solely for the information and use of the board of directors, management, and the RUS and supplemental lenders and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

Campbell, Myers & Rutledge, PLLC
Glasgow, Kentucky

March 26, 2015

