

**SOUTH CENTRAL RURAL TELECOMMUNICATIONS  
COOPERATIVE, INC.  
AND SUBSIDIARY**

---

**Report on Audit of Consolidated Financial Statements  
and Supplementary Information**

**For the Years Ended  
June 30, 2017 and 2016**



## CONTENTS

---

	<u>Pages</u>
Independent Auditors' Report	1-2
Financial Statements:	
Balance Sheets	3-4
Statements of Operations	5
Statements of Comprehensive Income	6
Statements of Patronage Capital and Other Equities	7
Statements of Cash Flows	8-9
Notes to Financial Statements	10-17
Supplementary Information:	
Independent Auditors' Report on Consolidating and Supplementary Information	18
Schedule I - 2017 Consolidating Balance Sheet	19
Schedule II - 2017 Consolidating Statement of Operations	20
Schedule III - 2016 Consolidating Balance Sheet	21
Schedule IV - 2016 Consolidating Statement of Operations	22
Statistical and Analytical Information	23-24
Independent Auditors' Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with <i>Government Auditing Standards</i>	25-26
Independent Auditors' Report on Compliance with Aspects of Contractual Agreements and Regulatory Requirements For Telecommunication Borrowers	27-29



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 ▪ Ryan Mosier, CPA ▪ Jenna B. Pace, CPA

## Independent Auditors' Report

Board of Directors  
South Central Rural Telecommunications  
Cooperative, Inc.  
Glasgow, Kentucky 42141

We have audited the accompanying consolidated financial statements of South Central Rural Telecommunications Cooperative, Inc. and subsidiary, which comprise the consolidated balance sheets as of June 30, 2017 and 2016, and the related consolidated statements of operations, 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 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 audits. 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 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 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 consolidated 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 consolidated financial statements.

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

## **Opinion**

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the respective financial position of South Central Rural Telecommunications Cooperative, Inc. and subsidiary, as of June 30, 2017 and 2016, and the results of their operations and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## **Other Matters**

### *Supplementary Information*

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements that collectively comprise South Central Rural Telecommunications Cooperative, Inc. and subsidiary's basic financial statements. The consolidating schedules on pages 18-22 and the statistical and analytical information on pages 23-24 are presented for purposes of additional analysis and are not a required part of the basic financial statements. This data is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic 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 on pages 18-22 and the statistical and analytical information on pages 23-24 is fairly stated in all material respects in relation to the basic financial statements as a whole.

## **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated September 25, 2017, on our consideration of the South Central Rural Telecommunications Cooperative, Inc. and subsidiary'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 South Central Rural Telecommunications Cooperative, Inc. and subsidiary's internal control over financial reporting and compliance.

*Campbell, Myers & Rutledge, PLLC*

Certified Public Accountants  
Glasgow, Kentucky

September 25, 2017

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
BALANCE SHEETS  
June 30, 2017 and 2016

---

ASSETS	<u>2017</u>	<u>2016</u>
Current assets:		
Cash and cash equivalents	\$ 4,455,632	\$ 3,374,693
Temporary cash investments	500,000	500,000
Accounts and notes receivable, less allowance for doubtful accounts of \$43,805 in 2017 and \$55,935 in 2016	2,250,435	2,351,218
Materials and supplies at average cost	2,525,986	2,659,477
Accrued interest receivable	4,859	4,859
Prepaid expenses	<u>6,518,550</u>	<u>2,995,945</u>
Total current assets	<u>16,255,462</u>	<u>11,886,192</u>
Other assets:		
Marketable securities	31,997,396	40,525,960
Nonregulated investments	800,225	823,666
Investment in affiliated companies	78,829,886	66,464,071
Other deferred charges	<u>1,644,990</u>	<u>1,422,384</u>
Total other assets	<u>113,272,497</u>	<u>109,236,081</u>
Telephone plant, at cost		
Telephone plant in service	211,467,374	210,472,184
Telephone plant under construction	<u>11,966,633</u>	<u>8,859,008</u>
Total	223,434,007	219,331,192
Less accumulated depreciation	<u>159,405,713</u>	<u>156,974,150</u>
Telephone plant, net	<u>64,028,294</u>	<u>62,357,042</u>
TOTAL ASSETS	<u>\$ 193,556,253</u>	<u>\$ 183,479,315</u>

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
 BALANCE SHEETS, CONCLUDED  
 June 30, 2017 and 2016

---

LIABILITIES AND MEMBERS' EQUITIES	<u>2017</u>	<u>2016</u>
Current liabilities:		
Accounts payable	\$ 5,308,692	\$ 5,200,433
Accrued expenses	<u>3,298,768</u>	<u>3,146,671</u>
Total current liabilities	<u>8,607,460</u>	<u>8,347,104</u>
Long-term liabilities:		
Deferred taxes	14,851,605	15,238,787
Other long-term liabilities	<u>12,568,134</u>	<u>10,873,628</u>
Total long-term liabilities	<u>27,419,739</u>	<u>26,112,415</u>
Members' equities:		
Patronage capital	43,155,347	46,334,548
Accumulated other comprehensive loss	(9,246,031)	(7,838,134)
Other equities	121,961,826	108,757,296
Other member capital	<u>1,657,912</u>	<u>1,766,086</u>
Total members' equities	<u>157,529,054</u>	<u>149,019,796</u>
TOTAL LIABILITIES AND MEMBERS' EQUITIES	<u>\$ 193,556,253</u>	<u>\$ 183,479,315</u>

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

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
 STATEMENTS OF OPERATIONS  
 For the Years Ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Operating revenues:		
Basic local network service	\$ 7,093,776	\$ 7,171,828
Network access services revenues	11,966,132	12,473,308
Carrier billing and collection	328,924	445,975
Miscellaneous	<u>1,208,314</u>	<u>1,169,138</u>
Total operating revenues	<u>20,597,146</u>	<u>21,260,249</u>
Operating expenses:		
Plant specific operations	5,080,433	4,969,775
Plant nonspecific operations	2,837,860	2,601,804
Depreciation and amortization	9,584,659	8,917,896
Customer operations	1,999,618	1,839,547
Corporate operations	2,434,217	3,070,295
Other operating taxes	<u>1,212,216</u>	<u>1,233,318</u>
Total operating expenses	<u>23,149,003</u>	<u>22,632,635</u>
Operating income	<u>(2,551,857)</u>	<u>(1,372,386)</u>
Nonoperating net income	24,667,967	15,140,671
Provision for income taxes	<u>(11,463,437)</u>	<u>(5,308,939)</u>
Income before interest charges	<u>10,652,673</u>	<u>8,459,346</u>
Nonregulated net income (loss)	<u>751,809</u>	<u>(368,363)</u>
Net income	<u>\$ 11,404,482</u>	<u>\$ 8,090,983</u>

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



SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
STATEMENTS OF COMPREHENSIVE INCOME  
For the Years Ended June 30, 2017 and 2016

---

	<u>2017</u>	<u>2016</u>
Net income	\$ 11,404,482	\$ 8,090,983
Other comprehensive income (loss)		
Postretirement benefit other than pension:		
Unrecognized gain/(loss) on assets	<u>(1,407,897)</u>	<u>1,041,215</u>
Comprehensive income	<u>\$ 9,996,585</u>	<u>\$ 9,132,198</u>

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

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
 STATEMENTS OF PATRONAGE CAPITAL AND OTHER EQUITIES  
 For the Years Ended June 30, 2017 and 2016

	Patronage Capital			Accumulated Other Comprehensive Income (Loss)	Other Equities
	Assignable	Assigned	Balance		
Balances, July 1, 2015	\$ (7,413,532)	\$ 57,499,606	\$ 50,086,074	\$ (8,879,349)	\$ 98,925,564
Distribution of patronage capital	-	(1,499,997)	(1,499,997)	-	-
Patronage capital assigned for the year ended December 31, 2015	2,276,953	(2,276,953)	-	-	-
Retirement of patronage capital of estates of deceased members	-	(510,855)	(510,855)	-	-
Transfer of unclaimed patronage capital	75	-	75	-	-
Postretirement benefit other than pension Unrecognized loss on assets	-	-	-	1,041,215	-
Recalculation of prior year allocated loss	-	-	-	-	-
Net income for the year ended June 30, 2016:					
Operating margins	(1,740,749)	-	(1,740,749)	-	-
Nonoperating margins	-	-	-	-	9,831,732
Balances, June 30, 2016	(6,877,253)	53,211,801	46,334,548	(7,838,134)	108,757,296
Distribution of patronage capital	-	(1,500,000)	(1,500,000)	-	-
Patronage capital assigned for the year ended December 31, 2016	1,002,079	(1,002,079)	-	-	-
Retirement of patronage capital of estates of deceased members	-	(181,358)	(181,358)	-	-
Transfer of unclaimed patronage capital	-	302,205	302,205	-	-
Postretirement benefit other than pension Unrecognized income on assets	-	-	-	(1,407,897)	-
Net income for the year ended June 30, 2017:					
Operating margins	(1,800,048)	-	(1,800,048)	-	-
Nonoperating margins	-	-	-	-	13,204,530
Balances, June 30, 2017	<u>\$ (7,675,222)</u>	<u>\$ 50,830,569</u>	<u>\$ 43,155,347</u>	<u>\$ (9,246,031)</u>	<u>\$ 121,961,826</u>

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

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
 STATEMENTS OF CASH FLOWS  
 For the Years Ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Cash flows from operating activities:		
Net income	\$ 11,404,482	\$ 8,090,983
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	11,565,560	10,712,009
Deferred taxes on income	(387,182)	(281,624)
Changes in operating assets and liabilities:		
Decrease (increase) in temporary cash investments	-	(100,000)
Decrease (increase) in accounts and notes receivable	100,783	(246,408)
Decrease (increase) in inventory	133,491	79,176
Decrease (increase) in prepaid expenses	(3,522,605)	756,190
Increase (decrease) in accounts payable	108,259	462,432
Increase (decrease) in accrued expenses	<u>152,097</u>	<u>138,113</u>
Net cash provided by operating activities	<u>19,554,885</u>	<u>19,610,871</u>
Cash flows from investing activities:		
Purchases of property, plant and equipment	(10,660,412)	(13,974,852)
Plant removal costs	(155,440)	(203,592)
Salvage recovered from retirement of plant	57,905	113,357
Decrease (increase) in nonregulated investment	23,441	33,473
Decrease (increase) in other deferred charges	(222,606)	3,102,316
(Increase) in investment in affiliated companies	(12,365,815)	(5,863,210)
Purchases of Marketable Securities	(9,587,763)	(13,443,125)
Redemptions of Marketable Securities	<u>14,229,565</u>	<u>13,839,575</u>
Net cash used in investing activities	<u>(18,681,125)</u>	<u>(16,396,058)</u>

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

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
 STATEMENTS OF CASH FLOWS, CONCLUDED  
 For the Years Ended June 30, 2017 and 2016

	<u>2017</u>	<u>2016</u>
Cash flows from financing activities:		
Distributions of patronage capital	\$ (1,500,000)	\$ (1,499,997)
Retirements of patronage capital	(181,358)	(510,855)
Principal payments to Federal Financing Bank	-	(1,606,221)
Increase (decrease) in long-term liabilities	1,694,506	(2,327,086)
Increase (decrease) in other member capital	(108,174)	417,570
Transfers of unclaimed patronage capital	<u>302,205</u>	<u>75</u>
Net cash provided (used) in financing activities	<u>207,179</u>	<u>(5,526,514)</u>
Net increase (decrease) in cash and cash equivalents	1,080,939	(2,311,701)
Cash and cash equivalents at beginning of year	<u>3,374,693</u>	<u>5,686,394</u>
Cash and cash equivalents at end of year	<u>\$ 4,455,632</u>	<u>\$ 3,374,693</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest (\$0 capitalized in 2017 and \$237,170 in 2016)	<u>\$ -</u>	<u>\$ 26,134</u>
Income taxes	<u>\$ 11,371,682</u>	<u>\$ 4,769,500</u>

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

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2017 and 2016

1. Summary of Significant Accounting Policies:

Nature of Business:

South Central Rural Telecommunications Cooperative, Inc. (the Cooperative), provides telephone service in a nine-county area of south central Kentucky. The Cooperative grants credit to customers, substantially all of whom are local residents and commercial businesses. The Cooperative maintains its accounts in accordance with the Uniform System of Accounts prescribed for telephone companies by the Federal Communications Commission. The consolidated financial statements include the accounts of the Cooperative and its wholly-owned subsidiary, South Central Telcom, LLC. All significant intercompany accounts and transactions have been eliminated.

Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of management to make 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 reported amounts of the revenues and expenses during the reporting period. Actual results could differ from those estimates.

Telephone Plant:

The telephone plant in service and under construction at June 30, 2017 and 2016 is stated substantially at original cost, which includes material, labor, transportation and such indirect items as engineering, supervision, employee fringe benefits and interest on funds used during construction. 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 the telephone plant as of June 30, 2017 and 2016:

	<u>2017</u>	<u>2016</u>
Organization	\$ 20,039	\$ 20,039
Land	720,374	714,831
Buildings	8,530,781	8,482,156
Central Office Equipment	49,220,524	54,803,419
Station Equipment	997,697	997,697
Cable and Wire Facilities	140,674,468	134,532,201
Furniture and Office Equipment	716,590	719,231
General Purpose Computers	4,364,298	4,252,096
Vehicles	6,087,083	5,814,994
Garage and Work Equipment	135,520	135,520
	<u>\$ 211,467,374</u>	<u>\$ 210,472,184</u>

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.

Depreciation for the consolidated financial statements for the years ended June 30, 2017 and 2016 was \$11,565,560 and \$10,712,009 respectively.

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
 NOTES TO FINANCIAL STATEMENTS  
 June 30, 2017 and 2016

1. Summary of Significant Accounting Policies, Continued:

Deregulated Customer Premises Equipment (CPE):

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.

Nonregulated Investments:

This balance reflects the Cooperative's permanent investment in deregulated CPE, net of applicable depreciation, plus deregulated inventory and accounts receivable, less deregulated accounts payable.

Following is a summary of net income (loss) from deregulated operations for the years ending June 30, 2017 and 2016, net of intercompany transactions:

	SCRTC		Telcom	
	2017	2016	2017	2016
Income from operations	\$ 20,714,072	\$ 19,517,161	\$ 4,654,091	\$ 4,565,332
Expenses	<u>19,871,608</u>	<u>19,885,524</u>	<u>4,744,746</u>	<u>4,456,151</u>
Net Income (loss)	<u>\$ 842,464</u>	<u>\$ (368,363)</u>	<u>\$ (90,655)</u>	<u>\$ 109,181</u>

Cash and Cash Equivalents:

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

Accounts and Notes Receivable:

The Cooperative estimates uncollectable accounts as a percentage of monthly revenues and compares this to invoices dated over 90 days when they are considered uncollectible. The Cooperative writes off receivables as a charge to the allowance for credit losses, in their estimation, it is probable that the receivable is worthless.

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.

Inventories:

Inventory is valued at average cost. Inventory consists of materials and expendable supplies held for future consumption or capitalization. The cost is recorded as an expense or capitalized as inventory items are consumed.

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2017 and 2016

1. Summary of Significant Accounting Policies, Concluded:

Investment in Affiliated Companies:

This balance reflects the Cooperative's investment in partnerships and limited liability companies with other telephone companies in Kentucky, for the purpose of providing cellular telephone services and local telephone service. The investment is accounted for using the equity method. Investments in affiliated companies are listed as follows:

	Percentage <u>Owned</u>	<u>2017</u>	<u>2016</u>
RSA #3 Partnership	25%	\$ 25,359,218	\$ 20,660,259
RSA #4 Partnership	50%	38,458,100	32,560,178
Cumberland Cellular Partnership	12.5%	9,245,605	7,751,450
Bluegrass Network LLC	20%	5,459,203	5,160,079
Bluegrass Telcom LLC	20%	307,760	332,105
		<u>\$ 78,829,886</u>	<u>\$ 66,464,071</u>

2. Cash and Temporary Investments:

All deposits are in various financial institutions and are carried at cost. Temporary Investments reflect Certificates of Deposit held at various financial institutions. Insured amounts reflect those covered by FDIC or by collateral pledged by the respective financial institutions.

	<u>2017</u>		<u>2016</u>	
	<u>Carrying Amount</u>	<u>Bank Balance</u>	<u>Carrying Amount</u>	<u>Bank Balance</u>
Insured	\$4,955,632	\$ 7,180,104	\$ 3,874,693	\$ 5,717,024
Uninsured:				
Uncollateralized	-	-	-	-
Total cash and temporary investments	<u>\$ 4,955,632</u>	<u>\$ 7,180,104</u>	<u>\$ 3,874,693</u>	<u>\$ 5,717,024</u>

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
 NOTES TO FINANCIAL STATEMENTS  
 June 30, 2017 and 2016

3. Pension Plan:

All eligible non-union employees of the Cooperative participate in the National Telephone Association (NTCA) Pension Plan (R&S Plan), a defined benefit pension plan qualified under section 401 and tax exempt under section 501(a) of the Internal Revenue Code. It is a multiemployer plan under the accounting standards. The Plan sponsor's identification number is 52-0741336 and the Plan Number is 333. Separate asset accounts are not maintained for participating employers. This means that assets contributed by one employer may be used to provide benefits to employees of other participating employers.

In October, 1988, the Cooperative approved the retroactive purchase of all prior service benefits as of December 31, 1988, at a cost of \$487,804. Contributions to the Plan for the years ended June 30, 2017 and 2016 were \$1,152,830 and \$1,228,528, respectively. 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 following table presents certain information regarding the Plan's status as a whole, derived from actuarial valuations performed as of the dates indicated:

	<u>Pension Benefits</u>	
	<u>January 1, 2017</u>	<u>January 1, 2016</u>
Fair value of plan assets	\$ 1,944,695,966	\$ 1,664,524,653
Present value of accumulated benefits	<u>(1,935,470,443)</u>	<u>(1,835,127,306)</u>
Overfunded/(Unfunded)	<u>\$ 9,225,523</u>	<u>\$ (170,602,653)</u>

	<u>Pension Benefits</u>	
	<u>January 1, 2017</u>	<u>January 1, 2016</u>
Weighted – average assumptions as of January 1:		
Valuation interest rate	7.00%	7.00%
Expected return on plan assets	7.00%	7.00%
Rate of compensation increase	age related	age related

On September 30, 2016, the Cooperative made a prepayment in the amount of \$3,948,353 for its R&S Plan. The prepayment amount is a cooperative's share of future contributions required to fund the R&S Plan's unfunded value of benefits earned to date using R&S Plan actuarial valuation assumptions. The prepayment amount will typically equal approximately 2.5 times a cooperative's annual R&S Plan required contribution. After making the prepayment, for most cooperatives the billing rate is reduced by approximately 25%, retroactive to January 1 of the year in which the amount is paid to the R&S Plan. The 25% differential in billing rates is expected to continue for approximately 15 years. However, several factors may have an impact on the differential in billing rates and the 15 year period. These factors include the following: changes in interest rates, asset returns and other plan experience different from expected as well as plan assumption changes.



SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS

June 30, 2017 and 2016

4. Postretirement Benefits:

The Cooperative sponsors a defined benefit plan that provides medical and life insurance coverage to retirees and their dependents. Participating retirees and dependents contribute 0% of the projected cost of coverage. Spouses of employees hired before January 1, 2015 are eligible. The plan is partially funded.

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 June 30, 2017 and 2016.

	<u>2017</u>	<u>2016</u>
Accumulated post-retirement benefit obligation, beginning	\$ 29,971,171	\$ 29,776,477
Service cost	1,047,607	910,914
Interest cost	1,439,444	1,329,233
Employer contributions	(788,894)	(777,742)
Actuarial loss/(gain)	2,299,820	(1,267,711)
Accumulated post retirement benefit obligation, ending	<u>\$ 33,969,148</u>	<u>\$ 29,971,171</u>
Fair value of plan assets - beginning of year	\$ 18,227,478	\$ 17,580,775
Employer contributions	788,894	777,742
Unrealized gains on assets	2,436,323	779,875
Benefits paid	(1,047,607)	(910,914)
Fair value of plan assets - end of year	<u>20,405,088</u>	<u>18,227,478</u>
Unfunded status	\$ 13,564,060	\$ 11,743,693
Unrecognized net actuarial loss	9,246,032	7,838,135
Net amount recognized	<u>\$ 4,318,028</u>	<u>\$ 3,905,558</u>
Unfunded status	\$ 13,564,060	\$ 11,743,693
Current liabilities	997,930	874,891
Noncurrent liabilities	<u>\$ 12,566,130</u>	<u>\$ 10,868,802</u>
Service cost	\$ 1,047,607	\$ 910,914
Interest cost	1,439,444	1,329,233
Amortization of net actuarial gain	378,351	320,514
Expected return on assets	(1,428,356)	(1,275,923)
Net periodic benefit cost	<u>\$ 1,437,046</u>	<u>\$ 1,284,738</u>
Net amount recognized (included in other comprehensive income)	<u>\$ (1,407,897)</u>	<u>\$ 1,041,215</u>
Amounts in other comprehensive income expected to be realized in the subsequent year - actuarial gain	<u>\$ 378,351</u>	<u>\$ 320,514</u>

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
 NOTES TO FINANCIAL STATEMENTS  
 June 30, 2017 and 2016

---

4. Postretirement Benefits, Concluded:

The discount rate used in determining the accumulated postretirement benefit obligation was 4.5% for the years ending June 30, 2017 and 2016, respectively.

Expected benefit payments from the plan for year ending June 30, 2017 total \$874,981.

The Cooperative contributes to a 401(h) trust that will be used to fund post-retirement benefits for future retirees. These monies are invested with NTCA, who manages such funds for cooperatives. NTCA invests in common stocks, high quality bonds, and US government securities. The estimated rates of return for plan assets are 7.00% and is based on recent historical performance. The investments of the assets are 98% in various Vanguard Funds and 2% in cash.

For measurement purposes, a 7.0% annual rate of increase in the per capita cost of covered health care benefits was used for the year ended June 30, 2017. The anticipated future rates are as follows:

2017	6.50%
2018	6.00%
2019	5.50%
2020	5.00%
2021	5.00%
2022-2026	5.00%

An additional 1% increase in the trend utilized for measurement purposes in 2017 would have resulted in an increase in the accumulated postretirement benefit obligation of approximately \$6.8 million.

The Trust Committee of the NTCA is responsible for the investment of the assets of the Alternative Funding Trusts. The asset allocation of the Trust's investments at 6/30/17 are as follows:

<u>Investment</u>	<u>Plan Percentage</u>
Vanguard Total Bond Market Index Fund	13.7%
Vanguard Total Stock Market Index Fund	24.7%
Vanguard High Yield Corporate Fund	8.1%
Vanguard FTSE All World Ex US Index Fund	26.2%
Vanguard REIT Index Fund	8.3%
Ishares ACWQI Minimum Volatility ETF	17.0%
Cash	<u>2.0%</u>
Total	100.0%

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2017 and 2016

5. Marketable Securities:

All debt securities of the Cooperative are considered to be held to maturity. The maturities of held to maturity investments and their approximate market values at June 30, 2017 and 2016, were as follows:

	Amortized Cost	Net Unrealized Gains (Losses)	Market Value
June 30, 2017	\$ 32,497,396	\$ (594,484)	\$ 31,902,912
June 30, 2016	\$ 41,025,960	\$ (84,358)	\$ 40,941,602

  

	Amortized Cost	Market Value
Due in one year or less (included in Temporary Cash Investments)	\$ 500,000	\$ 500,000
Due after one year	31,997,396	31,402,912
Balances, June 30, 2017	\$ 32,497,396	\$ 31,902,912

  

	Amortized Cost	Market Value
Due in one year or less (included in Temporary Cash Investments)	\$ 500,000	\$ 500,000
Due after one year	40,525,960	40,441,602
Balances, June 30, 2016	\$ 41,025,960	\$ 40,941,602

6. Income Taxes:

The Cooperative 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 2017 and 2016 consists of the following:

	2017	2016
Provision for Income Taxes:		
Current tax expense	\$ 11,850,618	\$ 5,590,563
Deferred tax (benefit)	(387,181)	(281,624)
Total	\$ 11,463,437	\$ 5,308,939

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2017 and 2016

---

6. Income Taxes, Concluded:

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

	<u>2017</u>	<u>2016</u>
Differences in depreciation methods	<u>\$ 14,851,605</u>	<u>\$ 15,238,787</u>

The Cooperative follows the recognition requirements for uncertain income tax positions as required by generally accepted accounting principles. The Cooperative has no tax position at June 30, 2017 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 Cooperative files income tax returns in the U.S. federal jurisdiction, and various state and local jurisdictions. The Cooperative is no longer subject to U.S. federal, state and local income tax examinations by tax authorities for years before 2014.

7. Subsequent Events:

Management has evaluated subsequent events thru September 25, 2017, the date which the financial statements were available to be issued.

## SUPPLEMENTARY 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 ▪ Ryan Mosier, CPA ▪ Jenna B. Pace, CPA

Independent Auditors' Report  
on Consolidating and Supplementary Information

Board of Directors  
South Central Rural Telecommunications  
Cooperative, Inc.  
Glasgow, Kentucky 42141

We have audited the consolidated financial statements of South Central Rural Telecommunications Cooperative, Inc. and subsidiary as of and for the years ended June, 2017 and 2016, and our report thereon dated September 25, 2017, which expressed an unmodified opinion on those financial statements appears on pages 1-2. Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The consolidating information presented on pages 18-22 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. The statistical and analytical information also is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. The consolidating and other supplementary 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 on pages 18-22 and the statistical and analytical information on pages 23-24, is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

*Campbell, Myers & Rutledge, PLLC*  
Certified Public Accountants  
Glasgow, Kentucky

September 25, 2017

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
SCHEDULE I – CONSOLIDATING BALANCE SHEET  
June 30, 2017

	South Central Rural Telecommunications Cooperative, Inc	South Central Telcom, LLC	Consolidating Entries	Consolidated Totals
<b>ASSETS</b>				
Current assets:				
Cash and cash equivalents	\$ 2,519,747	\$ 1,935,885	\$ -	\$ 4,455,632
Temporary cash investments	500,000	-	-	500,000
Accounts and notes receivable, less allowance for doubtful accounts of \$43,805	879,635	2,226,291	(855,491)	2,250,435
Materials and supplies at average cost	2,525,986	-	-	2,525,986
Accrued interest receivable	4,859	-	-	4,859
Prepaid expenses	6,518,550	-	-	6,518,550
Total current assets	<u>12,948,777</u>	<u>4,162,176</u>	<u>(855,491)</u>	<u>16,255,462</u>
Other assets:				
Marketable securities	31,997,396	-	-	31,997,396
Nonregulated investments	800,225	-	-	800,225
Investment in affiliated companies	94,645,842	-	(15,815,956)	78,829,886
Other deferred charges	1,440,836	204,154	-	1,644,990
Total other assets	<u>128,884,299</u>	<u>204,154</u>	<u>(15,815,956)</u>	<u>113,272,497</u>
Telephone plant, at cost (substantially all pledged as collateral on long- term debt to RUS):				
Telephone plant in service	187,589,344	23,878,030	-	211,467,374
Telephone plant under construction	11,966,633	-	-	11,966,633
Total telephone plant	<u>199,555,977</u>	<u>23,878,030</u>	<u>-</u>	<u>223,434,007</u>
Less accumulated depreciation	148,034,546	11,371,167	-	159,405,713
Telephone plant, net	<u>51,521,431</u>	<u>12,506,863</u>	<u>-</u>	<u>64,028,294</u>
<b>TOTAL ASSETS</b>	<u><b>\$ 193,354,507</b></u>	<u><b>\$ 16,873,193</b></u>	<u><b>\$ (16,671,447)</b></u>	<u><b>\$ 193,556,253</b></u>
<b>LIABILITIES AND MEMBERS' EQUITIES</b>				
Current liabilities:				
Accounts payable	\$ 5,106,946	\$ 1,057,237	\$ (855,491)	\$ 5,308,692
Accrued expenses	3,298,768	-	-	3,298,768
Total current liabilities	<u>8,405,714</u>	<u>1,057,237</u>	<u>(855,491)</u>	<u>8,607,460</u>
Long-term liabilities:				
Deferred taxes	14,851,605	-	-	14,851,605
Other long-term liabilities	12,568,134	-	-	12,568,134
Total long-term liabilities	<u>27,419,739</u>	<u>-</u>	<u>-</u>	<u>27,419,739</u>
Members' equities:				
Patronage capital	43,155,347	-	-	43,155,347
Accumulated other comprehensive loss	(9,246,031)	-	-	(9,246,031)
Other equities	121,961,826	15,815,956	(15,815,956)	121,961,826
Other member capital	1,657,912	-	-	1,657,912
Total members' equities	<u>157,529,054</u>	<u>15,815,956</u>	<u>(15,815,956)</u>	<u>157,529,054</u>
<b>TOTAL LIABILITIES AND MEMBERS' EQUITIES</b>	<u><b>\$ 193,354,507</b></u>	<u><b>\$ 16,873,193</b></u>	<u><b>\$ (16,671,447)</b></u>	<u><b>\$ 193,556,253</b></u>

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
SCHEDULE II – CONSOLIDATING STATEMENT OF OPERATIONS  
For the Year Ended June 30, 2017

	South Central Rural Telecommunications Cooperative, Inc	South Central Telcom, LLC	Consolidating Entries	Consolidated Totals
Operating revenues:				
Basic local network service	\$ 7,093,776	\$ -	\$ -	\$ 7,093,776
Network access services revenues	11,966,132	-	-	11,966,132
Carrier billing and collection	328,924	-	-	328,924
Miscellaneous	<u>1,208,314</u>	-	-	<u>1,208,314</u>
Total operating revenues	<u>20,597,146</u>	<u>-</u>	<u>-</u>	<u>20,597,146</u>
Operating expenses:				
Plant specific operations	5,080,433	-	-	5,080,433
Plant nonspecific operations	2,837,860	-	-	2,837,860
Depreciation and amortization	9,584,659	-	-	9,584,659
Customer operations	1,999,618	-	-	1,999,618
Corporate operations	2,434,217	-	-	2,434,217
Other operating taxes	<u>1,212,216</u>	<u>-</u>	<u>-</u>	<u>1,212,216</u>
Total operating expenses	<u>23,149,003</u>	<u>-</u>	<u>-</u>	<u>23,149,003</u>
Operating income	(2,551,857)	-	-	(2,551,857)
Nonoperating net income	24,577,312	-	90,655	24,667,967
Provision for income taxes	(11,463,437)	-	-	(11,463,437)
Nonregulated net income (loss)	<u>842,464</u>	<u>(90,655)</u>	<u>-</u>	<u>751,809</u>
Net Income	<u>\$ 11,404,482</u>	<u>\$ (90,655)</u>	<u>\$ 90,655</u>	<u>\$ 11,404,482</u>
Other comprehensive income (loss)				
Postretirement benefit other than pension:				
Unrecognized gain (loss) on assets	<u>(1,407,897)</u>	<u>-</u>	<u>-</u>	<u>\$ (1,407,897)</u>
Comprehensive income	<u>\$ 9,996,585</u>	<u>\$ (90,655)</u>	<u>\$ 90,655</u>	<u>\$ 9,996,585</u>



**SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY**  
**SCHEDULE III – CONSOLIDATING BALANCE SHEET**

June 30, 2016

	South Central Rural Telecommunications Cooperative, Inc	South Central Telcom, LLC	Consolidating Entries	Consolidated Totals
<b>ASSETS</b>				
<b>Current assets:</b>				
Cash and cash equivalents	\$ 2,078,634	\$ 1,296,059	\$ -	\$ 3,374,693
Temporary cash investments	500,000	-	-	500,000
Accounts and notes receivable, less allowance for doubtful accounts of \$55,935	987,732	2,204,066	(840,580)	2,351,218
Materials and supplies at average cost	2,659,477	-	-	2,659,477
Accrued interest receivable	4,859	-	-	4,859
Prepaid expenses	2,995,945	-	-	2,995,945
Total current assets	<u>9,226,647</u>	<u>3,500,125</u>	<u>(840,580)</u>	<u>11,886,192</u>
<b>Other assets:</b>				
Marketable securities	40,525,960	-	-	40,525,960
Nonregulated investments	823,666	-	-	823,666
Investment in affiliated companies	82,420,682	-	(15,956,611)	66,464,071
Other deferred charges	1,249,413	172,971	-	1,422,384
Total other assets	<u>125,019,721</u>	<u>172,971</u>	<u>(15,956,611)</u>	<u>109,236,081</u>
<b>Telephone plant, at cost (substantially all pledged as collateral on long- term debt to RUS):</b>				
Telephone plant in service	187,335,784	23,136,400	-	210,472,184
Telephone plant under construction	8,859,008	-	-	8,859,008
Total telephone plant	<u>196,194,792</u>	<u>23,136,400</u>	<u>-</u>	<u>219,331,192</u>
Less accumulated depreciation	147,185,290	9,788,860	-	156,974,150
Telephone plant, net	<u>49,009,502</u>	<u>13,347,540</u>	<u>-</u>	<u>62,357,042</u>
<b>TOTAL ASSETS</b>	<u><b>\$ 183,255,870</b></u>	<u><b>\$ 17,020,636</b></u>	<u><b>\$ (16,797,191)</b></u>	<u><b>\$ 183,479,315</b></u>
<b>LIABILITIES AND MEMBERS' EQUITIES</b>				
<b>Current liabilities:</b>				
Accounts payable	\$ 4,976,988	\$ 1,064,025	(840,580)	\$ 5,200,433
Accrued expenses	3,146,671	-	-	3,146,671
Total current liabilities	<u>8,123,659</u>	<u>1,064,025</u>	<u>(840,580)</u>	<u>8,347,104</u>
<b>Long-term liabilities</b>				
Deferred taxes	15,238,787	-	-	15,238,787
Other long-term liabilities	10,873,628	-	-	10,873,628
Total long-term liabilities	<u>26,112,415</u>	<u>-</u>	<u>-</u>	<u>26,112,415</u>
<b>Members' equities:</b>				
Patronage capital	46,334,548	-	-	46,334,548
Accumulated other comprehensive loss	(7,838,134)	-	-	(7,838,134)
Other equities	108,757,296	15,956,611	(15,956,611)	108,757,296
Other member capital	1,766,086	-	-	1,766,086
Total members' equities	<u>149,019,796</u>	<u>15,956,611</u>	<u>(15,956,611)</u>	<u>149,019,796</u>
<b>TOTAL LIABILITIES AND MEMBERS' EQUITIES</b>	<u><b>\$ 183,255,870</b></u>	<u><b>\$ 17,020,636</b></u>	<u><b>\$ (16,797,191)</b></u>	<u><b>\$ 183,479,315</b></u>

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC. AND SUBSIDIARY  
SCHEDULE IV – CONSOLIDATING STATEMENT OF OPERATIONS  
For the Year Ended June 30, 2016

	South Central Rural Telecommunications Cooperative, Inc	South Central Telcom, LLC	Consolidating Entries	Consolidated Totals
Operating revenues:				
Basic local network service	\$ 7,171,828	\$ -	\$ -	\$ 7,171,828
Network access services revenues	12,473,308	-	-	12,473,308
Carrier billing and collection	445,975	-	-	445,975
Miscellaneous	<u>1,169,138</u>	-	-	<u>1,169,138</u>
Total operating revenues	<u>21,260,249</u>	<u>-</u>	<u>-</u>	<u>21,260,249</u>
Operating expenses:				
Plant specific operations	4,969,775	-	-	4,969,775
Plant nonspecific operations	2,601,804	-	-	2,601,804
Depreciation and amortization	8,917,896	-	-	8,917,896
Customer operations	1,839,547	-	-	1,839,547
Corporate operations	3,070,295	-	-	3,070,295
Other operating taxes	<u>1,233,318</u>	-	-	<u>1,233,318</u>
Total operating expenses	<u>22,632,635</u>	<u>-</u>	<u>-</u>	<u>22,632,635</u>
Operating income	(1,372,386)	-	-	(1,372,386)
Nonoperating net income	15,140,671	258	(258)	15,140,671
Provision for income taxes	(5,308,939)	-	-	(5,308,939)
Nonregulated net income (loss)	<u>(368,363)</u>	<u>109,181</u>	<u>(109,181)</u>	<u>(368,363)</u>
Net Income	<u>\$ 8,090,983</u>	<u>\$ 109,439</u>	<u>\$ (109,439)</u>	<u>\$ 8,090,983</u>
Other comprehensive income (loss)				
Postretirement benefit other than pension:				
Unrecognized gain (loss) on assets	<u>1,041,215</u>	-	-	<u>\$ 1,041,215</u>
Comprehensive income	<u>\$ 9,132,198</u>	<u>\$ 109,439</u>	<u>\$ (109,439)</u>	<u>\$ 9,132,198</u>

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC.  
LIMITED DATA – SCRTC ONLY  
STATISTICAL AND ANALYTICAL INFORMATION  
June 30, 2017 and 2016

---

	2017	2016
<u>Telephone Plant in Service - June 30:</u>	\$ 187,589,344	\$ 187,335,784
Investment per subscriber - June 30	8,067	8,003
Investment per dollar of operating revenue	9.11	8.81
 <u>Depreciation Reserve - June 30:</u>	 148,034,546	 147,185,290
Percent of plant in service	78.91%	78.57%
Annual depreciation	9,584,659	8,917,896
Percent of annual depreciation to plant in service	5.11%	4.76%
 <u>Average Annual Revenue Per Subscriber:</u>		
Local service	305	306
Toll service and access charges	515	533
Total operating revenue	886	908
 <u>Number of Stations - June 30:</u>		
Residence:		
Main stations	20,354	20,420
Business:		
Main stations (access lines)	2,901	2,988
Total main stations	23,255	23,408

Computations involving number of subscribers are based on the number of subscribers at June 30.

SOUTH CENTRAL RURAL TELECOMMUNICATIONS COOPERATIVE, INC.  
LIMITED DATA – SCRTC ONLY  
STATISTICAL AND ANALYTICAL INFORMATION, CONCLUDED  
June 30, 2017 and 2016

	2017		2016	
	Amount	Percent	Amount	Percent
<u>For the year ended June 30,</u>				
Local network service	\$ 7,093,776	34.44%	\$ 7,171,828	33.73%
Network access and long-distance network service	11,966,132	58.10%	12,473,308	58.67%
Miscellaneous	<u>1,537,238</u>	<u>7.46%</u>	<u>1,615,113</u>	<u>7.60%</u>
Total operating revenue	<u>20,597,146</u>	<u>100.00%</u>	<u>21,260,249</u>	<u>100.00%</u>
Cost of telephone service, net of other income and expenses	<u>9,192,664</u>	<u>44.63%</u>	<u>13,169,266</u>	<u>61.94%</u>
Net income	<u>\$ 11,404,482</u>	<u>55.37%</u>	<u>\$ 8,090,983</u>	<u>38.06%</u>

	2017		2016	
	Amount	Percent	Amount	Percent
<u>Source of Funds Invested in</u>				
<u>Total Assets - June 30:</u>				
Members' equities	\$ 157,529,054	81.47%	\$ 149,019,796	81.32%
Long-term liabilities	27,419,739	14.18%	26,112,415	14.25%
Other liabilities	<u>8,405,714</u>	<u>4.35%</u>	<u>8,123,659</u>	<u>4.43%</u>
Total assets	<u>\$ 193,354,507</u>	<u>100.00%</u>	<u>\$ 183,255,870</u>	<u>100.00%</u>



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 ▪ Ryan Mosier, CPA ▪ Jenna B. Pace, CPA

Independent Auditors' 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  
South Central Rural Telecommunications  
Cooperative, Inc.  
Glasgow, Kentucky 42141

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 South Central Rural Telecommunications Cooperative, Inc. and subsidiary which comprise the consolidated balance sheets as of June 30, 2017 and 2016, and the related consolidated 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, and have issued our report thereon dated September 25, 2017.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered South Central Rural Telecommunications Cooperative, Inc. and subsidiary'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 South Central Rural Telecommunications Cooperative, Inc. and subsidiary's internal control. Accordingly, we do not express an opinion on the effectiveness of South Central Rural Telecommunications Cooperative, Inc. and subsidiary'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 South Central Rural Telecommunications Cooperative, Inc. and subsidiary'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  
Glasgow, Kentucky

September 25, 2017



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

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

Independent Auditors' Report on Compliance with Aspects  
of Contractual Agreements and Regulatory Requirements  
For Telecommunication Borrowers

Board of Directors  
South Central Rural Telecommunications  
Cooperative, Inc.  
Glasgow, Kentucky 42141

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 South Central Rural Telecommunications Cooperative, Inc. and subsidiary, which comprise the balance sheets as of June 30, 2017 and 2016, and the related statements of operations, comprehensive income, patronage capital and other equities, and cash flows for the years ended, and the related notes to the financial statements, and have issued our report thereon dated September 25, 2017. In accordance with *Government Auditing Standards*, we have also issued our report dated September 25, 2017, on our consideration of South Central Rural Telecommunications Cooperative, Inc. and subsidiary'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 South Central Rural Telecommunications Cooperative, Inc. and subsidiary 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 September 25, 2017, 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 South Central Rural Telecommunications Cooperative, Inc. and subsidiary'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 South Central Rural Telecommunications Cooperative, Inc. and subsidiary's accounting and records to indicate that South Central Rural Telecommunications Cooperative, Inc. and subsidiary 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 electric system;
- Disclose material related party transactions in the financial statements, in accordance with requirements for related parties in generally accepted accounting principles;
- Comply with the requirements for the detailed schedule of deferred debits and deferred credits which is as follows:

<b><u>Deferred Debits:</u></b>	<u>2017</u>	<u>2016</u>
Prepaid Insurance	\$ -	\$ 32,263
Job Orders	72,164	200,276
South Central Telcom Construction	<u>1,572,826</u>	<u>1,189,845</u>
	<u>\$ 1,644,990</u>	<u>\$ 1,422,384</u>

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

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

RSA #3 Partnership represents the Cooperative's 25% investment in a partnership which provides cellular telephone service. The Cooperative accounts for the investment on the equity basis.

RSA #4 represents the Cooperative's 50% investment in a partnership which provides cellular telephone service. The Cooperative accounts for the investment on the equity basis.

Cumberland Cellular Partnership represents the Cooperative's 12.5% investment in a partnership which provides cellular telephone 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.

Bluegrass Telcom 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.



	<u>RSA #3</u>	<u>RSA #4</u>	<u>RSA #5</u>	<u>Bluegrass Network LLC</u>	<u>Bluegrass Telecom LLC</u>	<u>Total</u>
Book Value of Investment as of 12/31/14	\$ 19,031,219	\$ 29,762,597	\$ 6,910,057	\$ 4,570,308	\$ 326,680	\$ 60,600,861
Dividends as of 12/31/15	\$ 2,387,500	\$ 4,300,000	\$ 807,344	\$ 200,000	\$ 50,850	
Undistributed Earnings/(Loss) as of 12/31/15	\$ 4,016,540	\$ 7,097,581	\$ 1,648,737	\$ 789,771	\$ 56,275	
Book Value of Investment as of 12/31/15	\$ 20,660,259	\$ 32,560,178	\$ 7,751,450	\$ 5,160,079	\$ 332,105	\$ 66,464,071
Dividends as of 12/31/16	\$ 3,614,000	\$ 6,268,800	\$ 1,153,250	\$ 200,000	\$ 87,048	
Undistributed Earnings/(Loss) as of 12/31/16	\$ 8,312,959	\$ 12,166,722	\$ 2,647,405	\$ 499,124	\$ 62,703	
Book Value of Investment as of 12/31/16	\$ 25,359,218	\$ 38,458,100	\$ 9,245,605	\$ 5,459,203	\$ 307,760	\$ 78,829,886

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

September 25, 2017

