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RECEIVED
MAR 16 2016
PUBLIC SERVICE
COMMISSION

March 15, 2016

VIA FEDERAL EXPRESS

Hon. James W. Gardner
Acting Executive Director
Kentucky Public Service Commission
211 Sower Blvd.
Frankfort KY 40601-8924

***Re: Tariff Filing of Foothills Rural Telephone Cooperative Corporation, Inc.*; Case No. 2016-00051**

Dear Acting Executive Director Gardner:

On behalf of Foothills Rural Telephone Cooperative Corporation, Inc., I have enclosed for filing with the Public Service of the Commonwealth of Kentucky one (1) original and ten (10) copies of the following documents.

1) Application for a General Adjustment in Rates;
2) Motion for Waiver of Certain Rate Application Filing Requirements; and
3) Petition for Confidential Treatment.

Thank you, and if you have any questions with regard to this matter, please call.

Sincerely yours,

DINSMORE & SHOHL LLP

Edward T. Depp

ETD/bmt
Enclosures

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED
MAR 16 2016
PUBLIC SERVICE COMMISSION

In the Matter of:

APPLICATION OF FOOTHILLS RURAL TELEPHONE COOPERATIVE CORPORATION, INC. FOR A GENERAL ADJUSTMENT IN RATES	)))	**CASE NO. 2016-00051**

APPLICATION

Applicant Foothills Rural Telephone Cooperative Corporation, Inc. ("Foothills"), by counsel, pursuant to KRS 278.180, 807 KAR 5:001, Sections 14 and 16, and 807 KAR 5:011, Section 6 and consistent with the Public Service Commission of the Commonwealth of Kentucky's (the "Commission") May 29, 2013 order in Case No. 2013-00190 (the "2013 Rate Floor Order") as well as with Foothills' November 26, 2014 rate floor proceeding in Case No. 2014-00328, files this application (the "Application") for authority to adjust its rates and charges for basic local exchange service and gives notice of its intention to increase the same rates and charges effective June 1, 2016.

INTRODUCTION

This Application for a rate increase is necessitated by an order from the Federal Communications Commission ("FCC") that fundamentally alters the cost structure of providing telecommunications services in high-cost rural areas, like those Foothills serves. *See In the Matter of Connect America Fund et al.,* Report and Order and Further Notice of Proposed Rulemaking, FCC 11-161 (Nov 18, 2011) ("ICC/USF Order"). For decades prior to the ICC/USF Order, high-cost carriers had received subsidies from the federal government's "Universal Service Fund" ("USF"). Those USF subsidies were intended to fulfill the Federal Communications Act's requirement that "[c]onsumers in all regions of the Nation, including . . .

those in rural, insular, and high cost areas, should have access to telecommunications and information services . . . that are available at rates that are reasonably comparable to rates charged for similar services in urban areas." 47 U.S.C. § 254(b)(3). The FCC found, however, that many rural consumers were paying rates that were less than those paid by consumers in urban areas. ICC/USF Order at ¶ 235. As a consequence, the FCC's ICC/USF Order sets a rate floor equal to the national average of local rates, plus state regulated fees. *Id.* at ¶ 238. The ICC/USF Order also "limit[s] high-cost support where local end-user rates plus state regulated fees" do not meet that national rate floor; those carriers' federal subsidies will be reduced "on a dollar-for-dollar basis . . . to the extent that [the] carrier's local rates (plus state regulated fees) do not meet the urban rate floor." *Id.* at ¶ 239.

On June 10, 2014, the FCC altered the schedule for the imposition of rate floor penalties, effectively requiring carriers to ensure that their 2016 rate floor obligations are met no later than June 1, 2016 (the "2014 Rate Floor Order"). *See In the Matter of Connect America Fund et al.*, Report and Order, Declaratory Ruling, Order, Memorandum Opinion and Order, Seventh Order on Reconsideration, and Further Notice of Proposed Rulemaking, FCC 14-54, ¶¶ 79-80.

Foothills' proposed rate adjustment is thus necessary to preserve its ability to receive these USF subsidies that are important to its ability to provide telephone and information services in its high-cost rural service territory. Without a minimum rate sufficient to meet the FCC's new rate floor, high-cost carriers like Foothills will lose significant federal funding that has historically allowed these carriers to provide service to the most costly, rural customers. That loss of federal funding will threaten the financial existence of these rural carriers like Foothills, who have important obligations under federal and state law as carriers of last resort. Moreover, the loss of those subsidies would increase the pressure for Foothills to raise its rates even higher than the federal rate floor sought here because any loss of federal funds would lead to a need for Foothills to make up that revenue directly from its customer-members.

* * * * * *

In support of its Application, Foothills states as follows:

1. Pursuant to 807 KAR 5:001, Section 14(1): (i) the full name of the applicant is Foothills Rural Telephone Cooperative Corporation, Inc.; (ii) the mailing address of the applicant is 1621 Kentucky Route 40 West / P.O. Box 240, Staffordsville, KY 41256-0240.; and (iii) the electronic mailing address of the applicant is RuthC@Foothills.coop.

2. Pursuant to 807 KAR 5:001, Section 14(2), Foothills states that it is currently in good standing in the Commonwealth of Kentucky, where it is incorporated. A certified copy of Foothills' Articles of Incorporation and all amendments thereto is on file with the Commission in Case No. 2013-00193 (Exhibit 2 to Application).

3. Pursuant to 807 KAR 5:001, Section 16(1)(b)(1), Foothills provides the following statement of the reason the adjustment is requested. Further details are provided in Exhibit 1 of this Application.

a. Foothills was established in 1950 as a not-for-profit, member-owned cooperative to provide local telephone service to business and individual members within the exchanges of Blaine, Chapman, Fallsburg, Flat Gap, Royalton, Salyersville, and Staffordsville ("Service Territory"). Foothills is a rural incumbent local exchange carrier serving parts of Lawrence and Johnson counties and all of Magoffin county in eastern Kentucky. At year-end 2015, Foothills provided 10,748 residential lines and 1,864 business lines to its members. Foothills is an eligible telecommunications carrier ("ETC") in the communities it serves and is also the carrier of last resort ("COLR") in its Service Territory. In 2015, Foothills received $ 3,745,245 from the HCLS

Fund to support its COLR responsibilities in its Service Territory, and anticipates receiving $2.7M in calendar year 2016. As a high cost company, all HCLS revenues are crucial for Foothills to continue to meet its COLR responsibilities and to bring advanced services to the communities it serves.

b. This proceeding was motivated by an order of the FCC that implemented "a rule to limit high-cost support where end-user rates do not meet a specified local rate floor." *See* ICC/USF Order at ¶ 235.

c. Under the rule, local exchange carriers such as Foothills must meet a specified rate floor in each year in order to be eligible to receive the maximum possible amount of HCLS funding from the FCC. Failure to meet the rate floor by the deadline will result in a reduction in HCLS funding that the carrier could have otherwise received for that year. ICC/USF Order at ¶¶ 133, 238-40. Therefore, Foothills requires an adjustment of its rates to comply with the 2014 Rate Floor Order, thereby maintaining eligibility for the fiscal year 2016 maximum amount of HCLS funding.

4. The requirements of 807 KAR 5:001, Section 16(1)(b)(2), are inapplicable because Foothills does not operate under an assumed name pursuant to KRS 365.015.

5. Pursuant to 807 KAR 5:001, Section 16(1)(b)(3), Foothills has attached its proposed tariff, in such form as is required by 807 KAR 5:011, as part of Exhibit 2. The proposed effective date of the proposed tariff is June 1, 2016, at least 30 days from the date the Application is filed.

6. Pursuant to 807 KAR 5:001, Section 16(1)(b)(4), Foothills has attached as part of Exhibit 2 its present tariff using italicizing, underscoring, and strikethroughs to show proposed revisions.

7. Pursuant to 807 KAR 5:001, Section 16(1)(b)(5), Foothills states that notice has been given in compliance with 807 KAR 5:001, Section 17, as described below:

a. Pursuant 807 KAR 5:001, Section 17(1), Foothills has posted at its place of business a copy of the Public Notice and will, within five days of the filing of the Application, post on its website a copy of the Public Notice and a hyperlink to the location on the Commission's website where the case documents are available. A copy of the Public Notice is attached hereto as part of Exhibit 3.

b. Pursuant to 807 KAR 5:001, Section 17(2), Foothills, which has more than twenty (20) customers and is not a sewage utility, has provided notice to its customers by including the notice with customer bills mailed no later than the date the Application is submitted to the Commission. A copy of the notice sent to customers is attached hereto as part of Exhibit 3.

c. Pursuant to 807 KAR 5:001, Section 17(3), an affidavit verifying Foothills' provision of the required notice to its customers is attached hereto as part of Exhibit 3.

d. Pursuant to 807 KAR 5:001, Section 17(4), Foothills states that the Public Notice attached to this Application as Exhibit 3 complies with all "Notice Content" requirements prescribed by regulation because it contains all of the following elements:

i. The proposed effective date and the date the proposed rates are expected to be filed with the Commission;

ii. The present rates and proposed rates for each customer classification to which the proposed rates will apply;

iii. The amount of the change requested in both dollar amounts and percentage change for each customer classification to which the proposed rates will apply;

iv. The effect upon the average bill for each customer classification for the proposed rate change in basic local service;

v. A statement that a person may examine this Application at Foothills' offices;

vi. A statement that a person may examine this Application at the Commission's offices located at 211 Sower Boulevard, Frankfort, Kentucky, Monday through Friday, 8:00 a.m. to 4:30 p.m., or through the Commission's Web site at http://psc.ky.gov;

vii. A statement that comments regarding the Application may be submitted to the Commission through its Web site or by mail to Public Service Commission, Post Office Box 615, Frankfort, Kentucky 40602;

viii. A statement that the rates contained in this notice are the rates proposed by Foothills but that the Commission may order rates to be charged that differ from the proposed rates contained in the notice;

ix. A statement that a person may submit a timely written request for intervention to the Public Service Commission, Post Office Box 615, Frankfort, Kentucky 40602, establishing the grounds for the request including the status and interest of the party; and

x. A statement that if the Commission does not receive a written request for intervention within thirty (30) days of initial publication or mailing of the notice, the Commission may take final action on the Application.

8. The requirements of 807 KAR 5:001, Section 16(1)(b)(6), are inapplicable because Foothills is not a water district.

9. Pursuant to 807 KAR 5:001, Section 16(2), Foothills states that it notified the Commission in writing of its intent to file the Application on January 19, 2016, at least thirty (30) days but not more than sixty (60) days prior to filing the Application. A copy of the notice of intent is included in Exhibit 4 of this Application. Pursuant to 807 KAR 5:001, Section 16(2)(a), the notice of intent stated that the Application will be supported by a historical test period. Pursuant to 807 KAR 5:001, Section 16(2)(c), Foothills sent by electronic mail a .pdf copy of the notice of intent to the Attorney General's Office of Rate Intervention (rateintervention@ag.ky.gov) upon filing it with the Commission. A copy of that email, including the attached notice of intent, is included as part of Exhibit 4 of this Application.

10. The provisions of 807 KAR 5:001, Section 16(3), are inapplicable because Foothills is not an electric utility.

11. Pursuant to 807 KAR 5:001, Section 16(4)(a), a narrative summary of the particular circumstances that justify and support Foothills' Application, including a statement of the reason the adjustment is required, is attached hereto as Exhibit 1 and is incorporated herein by reference. Exhibit 1 is filed subject to a Petition for Confidential Treatment pursuant to 807 KAR 5:001, Section 13, filed contemporaneously with this Application.

12. As more fully explained in Foothills' Motion for Waiver of Certain Rate Application Requirements ("Motion for Waiver") filed contemporaneously with this Application, Foothills seeks waiver of 807 KAR 5:001, Section 16(4)(b), requiring the applicant's witnesses' prepared testimony.

13. The requirements of 807 KAR 5:001, Section 16(4)(c) are inapplicable because Foothills has gross annual revenues in excess of $5,000,000.00.

14. Pursuant to 807 KAR 5:001, Section 16(4)(d), Foothills estimates that the total amount of revenue increase resulting from the proposed rate adjustment will be approximately $157,644.

15. The requirements of 807 KAR 5:001, Section 16(4)(e), are inapplicable because Foothills is not an electric, gas, sewage, or water utility.

16. Pursuant to 807 KAR 5:001, Section 16(4)(f), Foothills states that the proposed rate adjustment will increase the average affected customer bill by $2.00. Additional details regarding the anticipated impact on affected customers are set forth in Exhibit 1.

17. Pursuant to 807 KAR 5:001, Section 16(4)(g), Foothills states that its proposed rate increase will affect its Residential customer class. Foothills' analysis of customers' bills and the corresponding revenue impact are provided in Foothills' responses to the requirements of Section 16(4)(d) and 16(4)(f) in paragraphs 14 and 16 above.

18. Pursuant to 807 KAR 5:001, Section 16(4)(h), Foothills states that parts A and B of its 2014 RUS operating report, the most recently available to Foothills, containing its TIER calculation, which assesses Foothills' actual revenue position compared to its required operating revenues, are attached as Exhibit 5. To the extent the Commission believes this section imposes

additional requirements relevant to this Application, Foothills respectfully seeks waiver of those requirements for the reasons set forth in its accompanying Motion for Waiver.

19. As more fully explained in Foothills' Motion for Waiver, Foothills seeks waiver of 807 KAR 5:001, Section 16(4)(i), requiring a reconciliation of the rate base and capital used to determine revenue requirements.

20. Pursuant to 807 KAR 5:001, Section 16(4)(j), Foothills states that its current chart of accounts was provided in Case 2014-00328 (Exhibit 6 to the Application) and is unchanged.

21. Pursuant to 807 KAR 5:001, Section 16(4)(k), Foothills has attached its independent auditor's annual opinion report hereto as Exhibit 6. The other requirements of this section are inapplicable because Foothills' independent auditor has not indicated "the existence of a material weakness in [Foothills]'s internal controls."

22. The requirements in 807 KAR 5:001, Section 16(4)(l), are inapplicable because Foothills has not been audited by the FCC.

23. Pursuant to 807 KAR 5:001, Section 16(4)(m), Foothills states that its most recent PSC Form T is on file with the Commission.

24. Pursuant to 807 KAR 5:001, Section 16(4)(n), Foothills County states a schedule identifying current depreciation rates used by major plant accounts was provided in Case 2014-00328 and is unchanged. To the extent the Commission believes this section requires more information than Foothills has provided, Foothills seeks waiver of 807 KAR 5:001, Section 16(4)(n) for the reasons set for in its Motion for Waiver.

25. Pursuant to 807 KAR 5:001, Section 16(4)(o), requiring a schedule of detailed information regarding all software, programs, and models used to prepare the Application,

Foothills states that it utilized no specialized software, program, or models, and relied on Microsoft Word and Microsoft Excel to prepare the Application and supporting exhibits.

26. The requirements of 807 KAR 5:001, Section 16(4)(p), are inapplicable because Foothills has never made a stock or bond offering.

27. As more fully explained in Foothills' Motion for Waiver, Foothills seeks waiver of 807 KAR 5:001, Section 16(4)(q), requiring the annual report to shareholders or members with statistical supplements. Foothills does not prepare such documents and instead presents its financial results to its members at its annual meeting. To the extent the Commission believes this section imposes additional requirements relevant to this Application, Foothills respectfully seeks waiver of those requirements for the reasons set forth in its accompanying Motion for Waiver.

28. As more fully explained in Foothills' Motion for Waiver, Foothills seeks waiver of 807 KAR 5:001, Section 16(4)(r), requiring monthly managerial reports.

29. The requirements of 807 KAR 5:001, Section 16(4)(s), are inapplicable because Foothills is not required to file the U.S. Securities and Exchange Commission's Form 10-K, Form 8-K, or Form 10-Q.

30. The requirements of 807 KAR 5:001, Section 16(4)(t), are inapplicable because Foothills has not had any amounts charged or allocated to it by an affiliate or general or home office, and has not paid any monies to an affiliate or a general or home office during the test period or during the previous three (3) calendar years.

31. The requirements of 807 KAR 5:001, Section 16(4)(u), are inapplicable because Foothills is not an electric, gas, sewage, or water utility.

32. The requirements of 807 KAR 5:001, Section 16(4)(v), are inapplicable because Foothills has fewer than 50,000 access lines.

33. The requirements of 807 KAR 5:001, Section 16(5), are inapplicable because Foothills' Application does not include any pro forma adjustments. To the extent the Commission believes the requirements of this section apply to this Application, Foothills respectfully seeks waiver of those requirements for the reasons set forth in its accompanying Motion for Waiver.

34. The requirements of 807 KAR 5:001, Section 16(6), are inapplicable because Foothills is not requesting a general adjustment in rates supported by a fully forecasted test period.

35. The requirements of 807 KAR 5:001, Section 16(7), are inapplicable because Foothills is not requesting a general adjustment in rates supported by a fully forecasted test period.

36. The requirements of 807 KAR 5:001, Section 16(8), are inapplicable because Foothills is not requesting a general adjustment in rates supported by a fully forecasted test period.

37. Pursuant to ¶ 3.a of the 2013 Rate Floor Order, Foothills has provided an estimate of the annual revenue to be received in 2016 from HCLS in Exhibit 1, Attachment A.

38. Pursuant to ¶ 3.b of the 2013 Rate Floor Order, Foothills has provided an estimate of the annual revenue to be lost due to adjustment of terminating access rates in the "Financial Support for Filing" section of Exhibit 1.

39. Pursuant to ¶ 3.c of the 2013 Rate Floor Order, Foothills has provided an estimate of the annual revenue to be generated by the tariff changes in Exhibit 1 and in response to the requirements of 807 KAR 5:001, Section 16(4)(d), in paragraph 14 above.

40. Pursuant to ¶ 3.d of the 2013 Rate Floor Order, Foothills has provided an estimate of historical line counts in Exhibit 1, Attachment B. As more fully explained in Foothills' Motion for Waiver, Foothills seeks partial waiver of ¶ 3.d of the 2013 Rate Floor Order, insofar as it requests projected line losses beyond those provided in Exhibit 1.

41. Pursuant to ¶ 3.e of the 2013 Rate Floor Order, Foothills has provided historical and projected universal service support information in the narrative response of Exhibit 1 and in Attachment A thereto. As is certified annually to the Commission, these funds are used by Foothills to provide voice and advanced data services to its customers, thereby providing its communities with access to critical communications and broadband services.

42. Pursuant to ¶ 3.f of the 2013 Rate Floor Order, Foothills states that narrative support for the proposed rate adjustment is contained in this Application and in Exhibit 1.

WHEREFORE, Foothills Rural Telephone Cooperative Corporation, Inc., respectfully requests that the Public Service Commission of the Commonwealth of Kentucky enter a final order approving Foothills' proposed revisions to the applicable tariffs and grant all other relief to which it is entitled.

Respectfully submitted,

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Counsel to Foothills Rural Telephone Cooperative Corporation, Inc.

CERTIFICATE OF SERVICE

I certify that, on the date this Application was filed with the Kentucky Public Service Commission, a true and accurate copy of the foregoing was served by Federal Express or by hand delivery upon the persons listed below.

Kentucky Attorney General
Office of Rate Intervention
700 Capitol Avenue, Suite 118
Frankfort, Kentucky 40601-3449

On this the 15th day of March, 2016.

Counsel to Foothills Rural Telephone Cooperative Corporation, Inc.

10214680v1

Description and Reason for Filing

With this filing, Foothills Rural Telephone Cooperative Corporation, Inc. ("Foothills") proposes to increase its basic residential local service rates by $2.00, to $18.00 per month. Foothills also proposes to offset that increase by expanding its local calling area to include calling to Johnson, Lawrence and Magoffin Counties. This filing is in response to the November 18, 2011 order by the Federal Communications Commission that mandates minimum local residential service rate levels as a condition of continued receipt of certain federal universal service supports. In that Order[1] (the so-called "Transformation Order") the FCC required that local exchange rates be set at or above a rate floor of $10, as of June 1, 2012; $14 as of June 1, 2013, and an "urban rate" – at that time undefined – on or before June 1, 2014 ("2014 rate floor"). The Transformation Order mandated that companies with rate levels below the applicable rate floor be penalized with a dollar for dollar reduction in federal high cost loop support ("HCLS").

On March 20, 2014 the FCC released the results of its controversial urban rate floor survey[2] that established the 2014 rate floor of $20.46; if implemented, this floor would become the basis on which HCLS recipients below the floor would be subject to the loss of funding as required by the FCC's Transformation Order. On June 20, 2014 the FCC issued an Order on Reconsideration[3] that modified the proposed 2014 urban rate floor to allow for a phase-in of the residential rate floor. Under its revised implementation schedule, companies were given the option to implement the rates over a 4-year period:

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[1] *In the Matter of Connect America Fund et al.*, Report and Order and Further Notice of Proposed Rulemaking, FCC 11-161 (Nov 18, 2011)
[2] *Wireline Competition Bureau Announces Results of Urban Rate Survey for Voice Services; Seeks Comment on Petition for Extension of Time to Comply with New Rate Floor*, Public Notice, DA 14-384, Released March 20, 2014
[3] Report and Order, Declaratory Ruling, Order, Memorandum Opinion And Order, Seventh Order On Reconsideration, and Further Notice of Proposed Rulemaking, FCC 14-54 (June 10, 2014)

> Therefore, we waive the application of section 54.318(b) for lines reported July 1, 2014, with a rate of $14 or above. Commencing January 2, 2015 (reflecting rates as of December 1, 2014), and thereafter, through June 30, 2016, we waive section 54.318(b) to the extent reported lines are greater than or equal to $16. For the period between July 1, 2016, and June 30, 2017, we waive section 54.318(b) to the extent reported rates are greater than or equal to $18, or the 2016 rate floor, whichever is lower. For the period between July 1, 2017, and June 30, 2018, we waive section 54.318(b) to the extent reported rates are greater than or equal to $20, or the 2017 rate floor, whichever is lower.[4]

Proposed Revisions and Customer Impact

With this filing, Foothills' basic residential rates are proposed to rise to $18.00. Foothills does not propose any changes to its basic business services, which are not subject to the Transformation Order and which are, in any event, priced above the $18.00 residential rate floor. To offset this residential rate increase, Foothills proposes to expand its extended area service ("EAS") calling scope to all rate centers in the three counties in which it provides services. In doing so, both the company's residential and business subscribers will receive local calling to all of the rate centers in Foothills' operating area, as well any other rate centers that are in Johnson, Lawrence, or Magoffin Counties.

In expanding its EAS, Foothills will forego originating switched access revenues previously billed as interexchange access on these former toll routes. To terminate the traffic to exchanges outside of its network, Foothills will use a contracted interexchange carrier as its underlying service provider.

Foothills proposes to extend the EAS benefit to both its business and residential subscribers. Accordingly, this filing actually represents a cost reduction for its business customers who will enjoy EAS calling on routes previously subject to toll charges. Depending on their individual communities of interest, Foothills expects that, for many of its residential

[4] *Ibid.*, para. 80

subscribers, the expanded local calling will mitigate the local rate increase and may actually offer savings.

As shown in Attachment C of this Exhibit, Foothills estimates that the annual cost of this greatly expanded calling area will be approximately $100K per year. Even without these offsets, however, as shown in the financial support section of this Exhibit, the impact of the FCC's Transformation Order warrants the rate increase proposed in this filing.

Company Information

The full name and address of the company is Foothills Rural Telephone Cooperative Corporation, Inc., 1621 Kentucky Route 40 West / P.O. Box 240, Staffordsville, KY 41256-0240. Foothills was established in 1950 as a not-for-profit, member-owned cooperative to provide local telephone service to business and individual members within the exchanges of Blaine, Chapman, Fallsburg, Flat Gap, Royalton, Salyersville, and Staffordsville ("Service Territory"). Foothills is a rural incumbent local exchange carrier serving parts of Lawrence and Johnson counties and all of Magoffin county in eastern Kentucky. At year-end 2015, Foothills provided 10,748 residential lines and 1,864 business lines to its members.

Foothills is an eligible telecommunications carrier ("ETC") in the communities it serves and is also the carrier of last resort ("COLR") in its Service Territory. In 2015, Foothills received $ 3,745,245 from the HCLS Fund to support its COLR responsibilities in its Service Territory, and anticipates receiving $2.7M in calendar year 2016. As a high cost company, all HCLS revenues are crucial for Foothills to continue to meet its COLR responsibilities and to bring advanced services to the communities it serves.

A schedule of Foothills' quarterly high cost support is provided in Attachment A of this Exhibit. Historic access line counts, as reported to the National Exchange Carrier Association, are provided in Attachment B.

Financial Support for Filing

Foothills is making these changes because the FCC's Transformation Order requires that companies that fail to meet the rate floor be penalized with a reduction in loop support. Companies that fail to meet the 2015 rate floor will experience a dollar for dollar reduction in HCLS beginning in July, 2016. As shown below, Foothills is seeking to increase its local exchange rates by $2.00 but by doing so will retain approximately 9.7% of its total HCLS support, or $258K per year.

	Subscribers	Current Rate	FCC Floor	At Risk
Residential Based on year-end 2015	10,748	$ 16.00	$ 18.00	$ 257,952
Annual HCLS (See Attachment A of this Exhibit)				$ 2,668,128
Support at risk absent a rate increase				9.7%

Included in the FCC's Transformation Order is a requirement that carriers cap and reduce not only their reciprocal, state, and interstate inter-carrier compensation rates but also the revenues Foothills is allowed to collect. Under the formula specified in the Transformation Order, the FCC capped allowed terminating access revenues from inter-carrier compensation at fiscal year 2011[5] collected levels and established a phase-down of those allowed amounts over the subsequent 5 years. With this change, Foothills cannot collect more than its current capped revenue amount net 5% *each year*. As shown in the step down of Eligible Access Recovery, the

[5] October 1, 2010 through September 30, 2011.

cumulative FCC-mandated reduction in its access revenue recovery is [redacted] through the fiscal period ending June, 2015.

Access Cap and Reduction

	Access Cap	Reduction
FY2011 10/1-9/30	[redacted]	[redacted]
2012-2013 Fiscal Period	[redacted]	[redacted]
2013-2014 Fiscal Period	[redacted]	[redacted]
2014-2015 Fiscal Period	[redacted]	[redacted]
2015-2016 Fiscal Period	[redacted]	[redacted]
Cumulative Reduction	[redacted]	[redacted]

As shown in Attachment C of this Exhibit, based on a one-month sampling of calling patterns, Foothills estimates the monthly cost to expand its calling area, as measured in lost access and the cost to terminate services, at $100,288 per year. Accordingly this offset of its proposed residential rate increase is a net increase of $157,644. Foothills estimates that the revenue gain of its proposed local service rate increase is still significantly less than the reduction imposed by the FCC's cap of Eligible Access Recovery in the 2015-2016 fiscal period.

This is the third residential rate increase filed by Foothills to meet the residential rate floor. In its first rate floor filing, effective June 1, 2013, Foothills met the basic exchange rate floor by offsetting its $2 rate increases with the inclusion of Caller ID, a $3.50 service. Its 2014 rate floor filing, effective December 1, 2014, included additional features with the basic service line. Both those filings were expected to have a nominal impact on the company's net revenues at $23,518[6] and $28,900,[7] respectively. Inclusive of the net increase proposed here, the

[6] *In the Matter of Tariff Filing of Foothills Rural Telephone Cooperative Corporation, Inc.*, Ky. P.S.C. Case No. 2013-000193

[7] *In the Matter of Application of Foothills Rural Telephone Cooperative Corporation, Inc. for a General Adjustment In Rates,* Ky. P.S.C. Case No. 2014-00328

company's aggregate offsets to FCC mandated rate increases is less than $300K, well below its aggregate access reductions to date.

Summary

The FCC's Transformation Order continues to dramatically change the revenue sources historically available to rural telephone companies like Foothills to use in meeting their COLR obligation and to expand the availability of advanced broadband services to their customers. Unfortunately, for many of these affected companies, doing so requires upward pressure on local service rates. Foothills has attempted to offset this upward rate pressure by increasing the size of its EAS calling scope for all of its subscribers. As shown in this documentation, Foothills has no other realistic options available to it and requests that its tariff revisions be approved.

REDACTED

Foothills Rural Telephone Coop. Corp., Inc. **Exhibit 1**
Case 2016-00051

Attachments to this Exhibit:

Attachment A: Foothills' quarterly high cost support 2015-2016

Attachment B: National Exchange Carrier Association Report of Access Lines

Attachment C: Rate Design Impact Analysis

Foothills Rural Telephone Cooperative
Case 2016-00051

Exhibit 1, Attachment A

Report Cycle	State	SAC	Study Area Name	Connect America Fund ICC Monthly Support	HCL Monthly Support	ICLS Monthly Support	SNA Monthly Support	Total High Cost Monthly	HCL Quarterly Support
1Q15	KY	260406	FOOTHILLS RURAL COOP	$215,308	$ 303,824	$292,862	$ -	$ 811,994	$ 911,472
2Q15	KY	260406	FOOTHILLS RURAL COOP	$215,308	$ 317,667	$292,862	$ -	$ 825,837	$ 953,001
3Q15	KY	260406	FOOTHILLS RURAL COOP	$215,308	$ 313,462	$289,564	$ -	$ 818,334	$ 940,386
4Q15	KY	260406	FOOTHILLS RURAL COOP	$215,308	$ 313,462	$289,564	$ -	$ 818,334	$ 940,386
2015 Total High Cost Loop Support									$3,745,245

1Q16	KY	260406	FOOTHILLS RURAL COOP	$205,181	$ 223,477	$289,564	$ -	$ 718,222	$ 670,431
2Q16	KY	260406	FOOTHILLS RURAL COOP	$205,181	$ 221,211	$289,564	$ -	$ 715,956	$ 663,633
2016 Annualized Total High Cost Loop Support									$2,668,128

The Exhibit 1(B) attachment has been omitted from the public filing. It has been provided under a petition for confidential treatment

REDACTED

Foothills Rural Telephone Cooperative Corporation, Inc. **Exhibit 1, Attachment C**
Case 2016-00051

Rate Design Impact Analysis

Residential Lines (Dec 2015)	Demand	Rate Change	Per Month	Annualized
Residential Rate Change	10,748	$ 2.00	$ 21,496	$ 257,952

January 2016 calling sample	Demand	Per Month	Annualized
Origination includes stimulation and attempts	[redacted]		
On Network Usage			
Out of Area Usage			
Total converted Access Traffic			
Termination includes stimulation only			
On Network Usage Terminating Access			
Out of Area Usage - Underlying IXC			
Total converted Access Traffic			
Trunking to underlying carrier (per DS1)			
Estimated Annual Cost of Expansion			$ 100,288
Residential Revenues			$ 257,952
Net Revenue Gain / (Loss)			$ 157,664

Foothills Rural Telephone Coop. Corp., Inc. **Exhibit 2**
Case 2016-00051

- Proposed Tariff Pages (Proposed)
- Proposed Tariff Pages (Proposed with Black Line)

Proposed Tariff Pages (To be Filed)

5. BASIC LOCAL EXCHANGE SERVICE (Cont'd)

5.2 Local Calling Areas (cont'd)

5.2.2 List of Local Calling Exchanges

Exchange	Local Calling Area	
		(C)
Blaine	Blaine, Louisa, Chapman, Fallsburg, Flat Gap, Royalton, Salyersville, Staffordsville, Paintsville	
Chapman	Chapman, Louisa, Blaine, Fallsburg, Flat Gap, Royalton, Salyersville, Staffordsville, Paintsville	
Fallsburg	Fallsburg, Louisa, Blaine, Chapman, Flat Gap, Royalton, Salyersville, Staffordsville, Paintsville	
Flat Gap	Flat Gap, Staffordsville, Paintsville, Blaine, Chapman, Fallsburg, Royalton, Salyersville, Louisa	
Royalton	Blaine, Chapman, Fallsburg, Flat Gap, Louisa, Royalton, Salyersville, Staffordsville, Paintsville	
Salyersville	Blaine, Chapman, Fallsburg, Flat Gap, Louisa, Royalton, Salyersville, Staffordsville, Paintsville	
Staffordsville	Staffordsville, Flat Gap, Paintsville, Blaine, Chapman, Fallsburg, Royalton, Salyersville, Louisa	
		(C)

Issue Date:
Effective Date: June 1, 2016

Issued by: /s/ Ruth Conley
Ruth Conley, General Manager

By Authority of Order of the Public Service Commission in
Case No. 2016-00051 dated ___________.

5. BASIC LOCAL EXCHANGE SERVICE (Cont'd)

5.3 Basic Exchange Line Service

5.3.1 Description

Basic Line Service provides a Customer with a single, voice-grade telephonic communications channel that can be used to place or receive one call at a time. Basic Lines are provided for connection of Customer-provided single station sets or facsimile machines to the public switched telecommunications network. Each Basic Line may be configured into a rotary line hunt group with other Company-provided Basic Lines.

All Basic Exchange lines are equipped with caller number feature capability. Residential Exchange lines are equipped with Three-way Calling and Call Waiting as standard features.

5.3.2 Rates

Rates do not include a charge for instrument or other customer premises' wiring or equipment. Rates for additional services, including installation charges, are shown elsewhere in this Tariff.

	Monthly
Business Exchange Access Rate	\$19.40
Residential Exchange Access Rate	\$18.00 **(I)**

Foothills Rural Telephone Coop. Corp., Inc. **Exhibit 2**
Case 2016-00051

Proposed Tariff Pages (with Black Line)

5. BASIC LOCAL EXCHANGE SERVICE (Cont'd)

5.2 Local Calling Areas (cont'd)

5.2.2 List of Local Calling Exchanges

Exchange	Local Calling Area
	(C)
Blaine	Blaine, Louisa, Chapman, Fallsburg, Flat Gap, Royalton, Salyersville, Staffordsville, Paintsville
Chapman	Chapman, Louisa, Blaine, Fallsburg, Flat Gap, Royalton, Salyersville, Staffordsville, Paintsville
Fallsburg	Fallsburg, Louisa, Blaine, Chapman, Flat Gap, Royalton, Salyersville, Staffordsville, Paintsville
Flat Gap	Flat Gap, Staffordsville, Paintsville, Blaine, Chapman, Fallsburg, Royalton, Salyersville, Louisa
Royalton	Blaine, Chapman, Fallsburg, Flat Gap, Louisa, Royalton, Salyersville, Staffordsville, Paintsville ~~Magoffin County~~
Salyersville	Blaine, Chapman, Fallsburg, Flat Gap, Louisa, Royalton, Salyersville, Staffordsville, Paintsville ~~Magoffin County~~
Staffordsville	Staffordsville, Flat Gap, Paintsville, Blaine, Chapman, Fallsburg, Royalton, Salyersville, Louisa
	(C)

Issue Date:
Effective Date: June 1, 2016

Issued by: /s/ Ruth Conley
Ruth Conley, General Manager

By Authority of Order of the Public Service Commission in Case No. 2016-00051 dated ______.

5. BASIC LOCAL EXCHANGE SERVICE (Cont'd)

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5.3.2 Rates

Rates do not include a charge for instrument or other customer premises' wiring or equipment. Rates for additional services, including installation charges, are shown elsewhere in this Tariff.

	Monthly
Business Exchange Access Rate	\$19.40
Residential Exchange Access Rate	\$~~16.00~~18.00 (I)

Issue Date: ~~December 1, 2014~~
Effective Date: ~~November 30, 2014~~June 1, 2016

Issued by: /s/ Ruth Conley
Ruth Conley, General Manager

By Authority of Order of the Public Service Commission in Case No. 2014~~6~~-00328051 dated ~~November 26, 2014~~.

CUSTOMER NOTICE AFFIDAVIT

AFFIDAVIT

I, Ruth Conley, am a representative of Foothills Rural Telephone Coop. Corp., Inc. and am authorized to make this statement on its behalf.

I attest that the customer notice accompanying this affidavit was sent to all customers as a bill insert on the following dates: February 20, March 1, and March 10, 2016, in accordance with Section 17(2) of 807 KAR 5:001. I declare under penalty of perjury that the foregoing is true and correct.

Signature: Ruth Conley

Subscribed and sworn to me before this 10th day of March, 2016.

Susan Fairchild
Notary Republic

My commission expires: 3-31-2018

On or around March 10th, Foothills Rural Telephone Cooperative Corp, Inc., has or will file with the KY Public Service Commission a change in basic local service rates charged to its subscribers due to a Federal Communication Commission mandate. With this change, residential local service rates are proposed to increase $2, from $16 to $18. If approved by the PSC, the effective date of this rate change will be June 1, 2016. We anticipate the average local residential service bill increase will be 8%. Because we are expanding our free calling areas, for many of our members there may be a rate reduction based on where they call.

With this change, calls to all three counties in our service area will become local calls. You will enjoy free calling to Johnson, Lawrence and Magoffin Counties.

The need to modify basic service rates is mandated by changes enacted by the Federal Communications Commission which set minimal local service rate levels as a condition of continued receipt of federal high cost support that allows us to deploy fiber optic facilities and support advanced voice and broadband services. Because this support is vital to the economic health of our community, we have no choice but to request this rate modification.

You may examine this application at the offices of Foothills Rural Telephone Cooperative Corp., Inc., (dba Foothills Communications) located at 1621 KY Route 40 W, Staffordsville, KY 41256, during regular business hours or at the offices of the Kentucky Public Service Commission located at 211 Sower Boulevard, Frankfort, Kentucky, Monday through Friday, 8:00 a.m. to 4:30 p.m., or through the commission's Web site at http://psc.ky.gov.

Comments regarding the application may be submitted to the Public Service Commission through its Website or by mail to Public Service Commission, Post Office Box 615, Frankfort, Kentucky 40602. Rates contained in this notice are the rates proposed by the Company but the Public Service Commission may order rates to be charged that differ from the proposed rates contained in this notice.

You may submit a timely written request for intervention to the Public Service Commission, Post Office Box 615, Frankfort, Kentucky 40602, establishing the grounds for the request including the status and interest of the party. If the Commission does not receive a written request for intervention within thirty (30) days of initial publication or mailing of this notice, the Commission may take final action on the application.

Foothills TELEPHONE COOPERATIVE P. O. BOX 240 • 1621 KY HWY 40 W • STAFFORDSVILLE, KY 41256

January 14, 2016

Mr. Jeff Derouen, Executive Director
Kentucky Public Service Commission
211 Sower Boulevard, P.O. Box 615
Frankfort, KY 40602-0615

Dear Mr. Derouen:

Foothills Rural Telephone Coop. Corp., Inc. ("Foothills") gives this notice pursuant to 807 KAR 5:001 Section 16(2) of its intent to file no sooner than thirty (30) days from today, but not more than sixty (60) days from today, an application for a general adjustment in its rates. The general adjustment in rates will be supported by a twelve (12) month historical test period that may include adjustments for known and measurable changes.

The anticipated rate application is intended to meet the rate floor mandated in 47 CFR § 54.318, compliance with which is required to ensure that Foothills continues to receive high cost support that is essential to its operations. (See In the matter of Connect America Fund, Report and Order and Further Notice of Proposed Rulemaking, FCC 11-161 (Nov. 18, 2011).)

The FCC's June 10, 2014 Order (See Report and Order, Declaratory Ruling, Order, Memorandum Opinion And Order, Seventh Order On Reconsideration, and Further Notice of Proposed Rulemaking, FCC 14-54) requires Foothills to have reported line rates greater than or equal to $18, commencing July 1, 2016 (reflecting rates in effect as of June 1, 2016)[1].

A copy of this notice is being emailed to the Attorney General's Office of Rate Intervention by electronic mail at rateintervention@ag.ky.gov.

Please refer any questions to me at 606-297-3501 or via email at ruthc@foothills.coop.

Sincerely,

Ruth Conley

Ruth Conley
CEO/General Manager

Cc via email: Jim Stevens, KY PSC
Eileen Bodamer, Bodamer Consulting

[1] Paragraph 80.

PHONE: 606-297-3501 • FAX: 606-297-2000 • E-MAIL: frtcc@foothills.net

Eileen Bodamer

From:	Susan Fairchild <susan@foothills.coop>
Sent:	Thursday, January 14, 2016 8:27 AM
To:	rateintervention@ag.ky.gov; wjstevens@ky.gov
Cc:	Eileen Bodamer
Subject:	Notice of Intent
Attachments:	Notice of Intent.pdf

Attached is our Notice of Intent to file a rate adjustment to meet the mandated rate floor. Please contact me with any questions.

Thanks,
Susan

Susan Fairchild
Chief Operations Officer
Foothills Communications

FOOTHILLS
COMMUNICATIONS

phone: 606-297-9115 | **fax**: 606-297-9615
email: susan@foothills.coop | **website:** www.foothills.net

Foothills Rural Telephone Cooperative Corporation, Inc.
Case 2016-00051

Exhibit 5

According to the Paperwork Reduction Act of 1995, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid OMB control number. The valid OMB control number for this information collection is xxxx. The time required to complete this information collection is estimated to average x hours per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information.

USDA-RUS	This data will be used by RUS to review your financial situation. Your response is required by 7 U.S.C. 901 et seq. and, subject to federal laws and regulations regarding confidential information, will be treated as confidential.
FINANCIAL AND STATISTICAL REPORT FOR BROADBAND BORROWERS	BORROWER NAME Foothills Rural Telephone Cooperative Corporation, I
	ADDRESS Staffordsville, Kentucky
INSTRUCTIONS-Submit report to RUS within 15 days after close of the period.	PERIOD ENDING: December, 2015 — BORROWER DESIGNATION: KY1108

CERTIFICATION

We hereby certify that:

1. the entries in this report are in accordance with the accounts and other records of the system and reflect the status of the system to the best of our knowledge and belief; and
2. we have fulfilled our obligations under the Loan Documents throughout the year in all material respects

ALL INSURANCE REQUIRED BY 7 CFR PART 1788, CHAPTER XVII, RUS, WAS IN FORCE DURING THE REPORTING PERIOD AND RENEWALS HAVE BEEN OBTAINED FOR ALL POLICIES.

- [x] All of the obligations under the RUS loan documents have been fulfilled in all material respects.
- [ ] There has been a default in the fulfillment of the obligations under the RUS loan documents. Said default(s) is/are specifically described in the notes section of this report.

RUTH CONLEY

CEO/GM

01/20/2016

DATE

PART A. BALANCE SHEET

ASSETS	BALANCE END OF PERIOD	LIABILITIES AND STOCKHOLDERS' EQUITY	BALANCE END OF PERIOD
CURRENT ASSETS		**CURRENT LIABILITIES**	
1. Cash and Equivalents	16,833,618	16. **Accounts Payable**	1,919,598
2. Cash-RUS Construction Fund		17. **Notes Payable**	
3. Accounts Receivable	3,357,841	18. **Current Mat. L/T Debt - RLIS**	168,000
4. Notes Receivable		19. **Current Mat. UT Debt-Other**	4,000,000
5. Materials and Inventory	1,280,307	20. **Current Mat.-Capital Leases**	
6. Other Current Assets	792,765	21. **Other Current Liabilities**	978,606
7. **Total Current Assets (1 thru 6)**	22,264,531	22. **Total Current Liabilities (16 thru 21)**	7,066,204
NONCURRENT ASSETS		**LONG-TERM DEBT**	
8. **Investment in Affiliated Companies**	26,507,365	23. Funded Debt-RUS Notes	4,907,380
9. Other Noncurrent Assets	1,575,301	24. Funded Debt-RTB Notes	
PLANT, PROPERTY, AND		25. Funded Debt-FFB Notes	
EQUIPMENT		26. Funded Debt-Other	3,115,737
10. Telecom. Plant-in-Service	122,011,872	**Total Long-Term**	
		27. **Debt (23 thru 26)**	8,023,117
11. Plant Under Construction	5,988,598	**OTHER LIAB. & DEF. CREDITS**	
12. Plant Adj., Nonop. Plant, & Goodwill		28. Other Long-Term Liabilities	4,220,046
13. Less Accumulated Depreciation	74,529,202	**EQUITY**	
Net Plant		29. Cap. Stock Outstand. & Subscribed	609,556
14. **(10 thru 12 less 13)**	53,471,268	30. Additional Paid-in-Capital	
		31. Membership and Cap. Certificates	
		32. Patronage Capital Credits	60,561,051
		33. Retained Earnings or Margins	23,338,491
		34. **Total Equity (29 thru 34)**	84,509,098
TOTAL ASSETS		**TOTAL LIABILITIES AND**	
15. **(7+8+9+14)**	103,818,465	35. **EQUITY (22+27+28+34)**	103,818,465

Total Equity = 81.4 **% of Total Assets**

USDA-RUS **FINANCIAL AND STATISTICAL REPORT FOR BROADBAND BORROWERS**	BORROWER DESIGNATION KY1108
	PERIOD ENDING December, 2015

PART B. STATEMENTS OF INCOME AND RETAINED EARNINGS OR MARGINS

ITEM	YEAR-TO-DATE
1. Local Network Services Revenues	
a. Voice	3,471,127
b. Video	1,390,473
c. Internet	
i. Broadband	2,780,945
ii. Other	
2. Network Access Services and Long Distance Revenues	12,717,434
3. Miscellaneous Revenues	929,169
4. Other Operating Income	
5. Uncollectible Revenues	24,000
6. Net Operating Revenues (11 thru 4 less 5)	21,265,148
7. Plant Specific Operations Expense	5,435,524
8. Plant Nonspecific Operations Expense *(Excluding Depreciation* & Amortization)	2,156,211
9. Customer Operations Expense	1,795,060
10. Corporate Operations Expense	1,896,077
11. Other Operating Expenses	
12. Total Operating Expenses (7 thru 11)	11,282,872
13. Operating Income or Margins (6 less 12)	9,982,276
14. Nonoperating/Nonregulated Net Income	(664,593)
15. EBIDTA (13 + 14)	9,317,683
16. Depreciation Expense	5,004,805
17. Amortization Expense	
18. EBIT (15 - 16 - 17)	4,312,878
19. Interest on Funded Debt	505,310
20. Other Interest Expense	8,733
21. Taxes	
a. Property	1,121,409
b. Income	2,742
22. Total Net Income or Margins (18-19-20-21)	2,674,684
23 Dividends Declared (Common)	
24 Dividends Paid	1,112,583
25 Transfers to Patronage Capital	
26 Principal Payments on Long Term Debt and Capital Leases	4,179,692
27 TIER (19 + 20 + 22) / (19 + 20)	6.20

Kentucky 522

Foothills Rural Telephone Cooperative and Subsidiary

Staffordsville, Kentucky

Audited Financial Statements
December 31, 2014 and 2013

Alan M. Zumstein
Certified Public Accountant
1032 Chetford Drive
Lexington, Kentucky 40509

CONTENTS

ALAN M. ZUMSTEIN
CERTIFIED PUBLIC ACCOUNTANT

1032 CHETFORD DRIVE
LEXINGTON, KENTUCKY 40509
(859) 264-7147
zumstein@windstream.net

MEMBER
• AMERICAN INSTITUTE OF CPA'S
• KENTUCKY SOCIETY OF CPA'S
• INDIANA SOCIETY OF CPA'S
• AICPA DIVISION FOR FIRMS

Independent Auditor's Report

To the Board of Directors
Foothills Rural Telephone Cooperative

Report on the Financial Statements

I have audited the accompanying consolidated financial statements of Foothills Rural Telephone Cooperative and Subsidiary, which comprise the balance sheets as of December 31, 2014 and 2013, and the related statements of revenue and comprehensive income, changes in 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 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

My responsibility is to express an opinion on these financial statements based on my audits. I did not audit the financial statements of East Kentucky Network, LLC. As discussed in Note 3, these financial statements account for an investment in East Kentucky Network, LLC under the equity method. The investment was $20,864,241 and $20,805,872 at December 31, 2014 and 2013 respectively, and the equity in its net margins was $1,069,928 and $2,075,249 for the years then ended. The financial statements of East Kentucky Network, LLC were audited by other auditors, whose report has been furnished to me, and my opinion, insofar as it relates to amounts for East Kentucky Network, LLC is based solely on the report of the other auditors. I conducted my 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 I plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's reparation 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, I express no such opinion. An audit also includes evaluating the appropriateness of

To the Board of Directors

accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

I believe the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Opinion

In my opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Foothills Rural Telephone Cooperative and Subsidiary as of December 31, 2014 and 2013, 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 Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, I have also issued a report dated March 3, 2015, on my consideration of Foothills Rural Telephone Cooperative's internal control over financial reporting and my 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 my testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the 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 internal control over financial reporting and compliance.

Report on Supplemental Information

My audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplementary information included in the consolidated financial statements is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from and related directly to underlying accounting and other records used to prepare the basic financial statements. The 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 my opinion, the information is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Alan M. Zumstein

Alan M. Zumstein, CPA
March 3, 2015

Foothills Rural Telephone Cooperative and Subsidiary
Consolidated Balance Sheets, December 31, 2014 and 2013

Assets	2014	2013
Current Assets:		
Cash and cash equivalents	$ 16,173,152	$ 14,689,891
Accounts receivable, less allowance for 2014 of $53,096 and 2013 of $94,550	681,716	674,410
Other accounts receivable	1,531,275	1,982,313
Materials and supplies, at average cost	1,213,807	1,276,242
Prepayments	559,296	345,748
	20,159,246	18,968,604
Other Assets:		
Investment securities available for sale	5,060,642	5,055,794
Investment in associated organization	20,864,241	20,805,872
Nonregulated investments	1,811,009	2,077,657
	27,735,892	27,939,323
Utility Plant, at original cost:		
In service	123,737,323	121,392,352
Under construction	6,784,630	4,099,188
	130,521,953	125,491,540
Less accumulated depreciation	72,902,441	68,016,031
	57,619,512	57,475,509
Total	$ 105,514,650	$ 104,383,436
Liabilities and Member's Equities		
Current Liabilities:		
Accounts payable	$ 1,237,218	$ 1,923,031
Current portion of long term debt	4,100,000	4,100,000
Customer deposits	207,506	213,606
Other current and accrued expenses	1,520,959	1,452,388
	7,065,683	7,689,025
Long Term Debt	11,247,584	13,902,908
Accrued Postretirement Benefits	4,065,784	4,019,015
Members' Equities:		
Memberships and capital investment	628,314	641,065
Patronage capital and retained earnings	84,866,941	80,641,247
Donated capital	124,537	124,537
Accumulated other comprehensive income	(2,484,193)	(2,634,361)
	83,135,599	78,772,488
Total	$ 105,514,650	$ 104,383,436

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

Consolidated Statements of Revenue and Comprehensive Income
for the years ended December 31, 2014 and 2013

	2014	2013
Operating Revenue:		
Basic local network services	$ 6,450,616	$ 5,572,725
Network access services	14,721,980	16,606,962
Billing and collection	482,228	510,982
Miscellaneous	902,826	685,888
Less provision for uncollectibles	(74,000)	(121,275)
	22,483,650	23,255,282
Operating Expenses:		
Plant specific operations	5,274,275	5,520,815
Plant nonspecific operations	2,038,640	1,974,496
Depreciation	5,726,805	7,012,306
Customer operations	1,717,401	1,649,224
Corporate operations	1,629,008	1,590,294
Taxes	1,380,356	1,334,543
	17,766,485	19,081,678
Operating margins	4,717,165	4,173,604
Nonoperating Margins		
Other nonoperating income	1,255,612	2,276,763
Non regulated activities	166,461	1,298,812
	1,422,073	3,575,575
Margins before interest charges	6,139,238	7,749,179
Interest Charges:		
Interest on long-term debt	615,659	698,699
Other	10,177	10,593
	625,836	709,292
Net Margins	5,513,402	7,039,887
Other Comprehensive Income:		
Postretirement benefits	150,168	150,168
Total Comprehensive Income	$5,663,570	$7,190,055

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

Statement of Changes in Consolidated Members' Equity
for the years ended December 31, 2013 and 2014

		Patronage Capital							Accumulated Other Comprehensive Income	Total Members' Equity
	Memberships	Assigned	Assignable	Unassigned	Unlocated	Retirements	Total	Other Equity		
Balance - Beginning of year	$ 651,075	$ 72,520,332	$ 7,113,073	$ 17,799,854	$ 1,376,726	$ (24,098,234)	$ 74,711,751	$124,537	$ (2,784,529)	$ 72,702,834
Allocate margins		5,747,134	(7,113,073)	1,645,439	(279,500)		-			-
Comprehensive income:										
Net margins			7,039,887				7,039,887			7,039,887
Postretirement benefit obligation										
Amortization									150,168	
Adjustment										150,168
Total comprehensive income										7,190,055
Net change in memberships	(10,010)									(10,010)
Refunds of capital credits						(1,110,391)	(1,110,391)			(1,110,391)
Other equities							-	-		-
Balance-December 31, 2013	641,065	78,267,466	7,039,887	19,445,293	1,097,226	(25,208,625)	80,641,247	124,537	(2,634,361)	78,772,488
Allocate margins		5,409,321	(7,039,887)	1,645,440	(14,874)		-			-
Comprehensive income:										
Net margins			5,513,402				5,513,402			5,513,402
Postretirement benefit obligation										
Amortization									150,168	
Adjustment										150,168
Total comprehensive income										5,663,570
Net change in memberships	(12,751)									(12,751)
Refunds of capital credits						(1,256,289)	(1,256,289)			(1,256,289)
Other equities					(2,552)	(28,867)	(31,419)	-		(31,419)
Balance-December 31, 2014	$ 628,314	$ 83,676,787	$ 5,513,402	$ 21,090,733	$ 1,079,800	$ (26,493,781)	$ 84,866,941	$124,537	$ (2,484,193)	$ 83,135,599

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

Consolidated Statements of Cash Flows

for the years ended December 31, 2014 and 2013

	2014	2013
Cash Flows from Operating Activities:		
Net margins	$ 5,513,402	$ 7,039,887
Adjustments to reconcile to net cash provided by operating activities:		
Depreciation	5,726,805	7,012,306
Accrued postretirement benefits	196,937	208,206
Income from subsidiary	(1,072,623)	(2,077,945)
Net change in current assets and liabilities:		
Receivables	359,658	336,924
Materials	62,435	(222,631)
Prepayments	(213,548)	16,055
Payables	(601,739)	50,392
Customer deposits	(6,100)	2,897
Other current and accrued liabilities	68,571	55,054
	10,033,798	12,421,145
Cash Flows from Investing Activities:		
Construction of plant	(5,782,297)	(3,746,238)
Salvage recovered from plant	(88,511)	(70,596)
Nonregulated investments	266,648	302,316
Investment in associated organizations	1,014,254	1,294,774
Change in investment securities	(4,848)	682,268
	(4,594,754)	(1,537,476)
Cash Flows from Financing Activities:		
Net increase in memberships and other equities	(44,170)	(10,010)
Retirements of capital credits	(1,256,289)	(1,110,391)
Advances on long term debt	1,472,737	2,213,902
Payments on long term debt	(4,128,061)	(4,059,644)
	(3,955,783)	(2,966,143)
Net increase in cash balances	1,483,261	7,917,526
Cash and cash equivalents - beginning	14,689,891	6,772,365
Cash and cash equivalents - end	$ 16,173,152	$ 14,689,891
Supplemental disclosures of cash flows information:		
Interest on long-term debt	$ 615,659	$ 698,699

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

Notes to Financial Statements, continued

Note 1 Summary of Significant Accounting Policies

Foothills Rural Telephone Cooperative (the Cooperative) maintains its records in accordance with policies prescribed or permitted by the Kentucky Public Service Commission (PSC) and the United States Department of Agriculture, Rural Utilities Service (RUS) Uniform System of Accounts, which conform in all material respects with generally accepted accounting principles in all material respects. The more significant of these policies are as follows:

Principles of Consolidation The consolidated financial statements include the accounts of the Cooperative and its wholly-owned subsidiary, Cellular Services, LLC (Cellular Services). All significant inter-company accounts and transactions have been eliminated.

Cash and Cash Equivalents The Cooperative considers all short-term, highly liquid investments with original maturities of three months or less to be cash equivalents.

Off Balance Sheet Risk The Corporation has off-balance sheet risk in that they maintain cash deposits in financial institutions in excess of the amounts insured by the Federal Deposit Insurance Corporation (FDIC). At December 31, 2014, the financial institutions reported deposits in excess of the $250,000 FDIC insured limit on several of the accounts. Deposits and repurchase agreements in excess of the FDIC limits are 100% secured with collateral from each of the respective financial institutions.

Telecommunications Revenue Recognition Revenues are recognized when earned regardless of the period in which they are billed. Bills are sent to customers on credit based on three (3) monthly billing cycles, with local service being billed a month in advance of service. Sales are concentrated in portions of five (5) southeastern Kentucky counties. Payments are due 20 days from the date of billing, at which time a disconnect notice is sent with payment to be within 10 days. The allowance for uncollectible accounts is based on the aging of accounts receivable. Accounts are written off when they are deemed to be uncollectible. There were no customers whose individual account balance exceeded 10% of outstanding accounts receivable at December 31, 2014 or 2013. The number of access lines was 12,921 at 2014 and 12,951 at 2013.

Interstate revenues are recognized on the cost basis recovery method. Compensation for intrastate/interlata service is received through tariffed access charges as filed with the FCC. These access charges are billed to the interlata long distance carrier and retained by the Cooperative.

Video Revenue Recognition Cellular Services' headend equipment will allow the Cooperative with the capabilities to provide expanded video services with over 200 channels, high definition television, and Video on Demand. The monthly charge will be based on the capacity utilized by Foothills Telephone and other unrelated companies.

Fiber to the Home Activities The Cooperative has launched an expanded services network. This network establishes the Cooperative as a full service network (FSN) provider allowing it to provide expanded video services with over 200 channels, high definition television and Video on Demand. It also is able to provide high speed internet, virtual private networks and voice on internet protocol (VoIP). This is accomplished through Fiber to the Home (FTTH) technology. The Cooperative purchases cable transmissions from networks at various amounts based on the number of customers receiving the service.

Utility Taxes Foothills Telephone and Cellular Services' is required to collect, on behalf of taxing authorities, excise taxes, sales, school taxes, and franchise fees. Foothills Telephone and Foothills Telecom's policy is to exclude taxes from revenue when collected and expenses when paid and instead, record collection and payment of taxes through a liability account.

Notes to Financial Statements, continued

Note 1 Summary of Significant Accounting Policies, continued

Fair Value Measurements The Fair Value Measurements and Disclosures Topic of the FASB ASC 820, *Fair Value Measurements and Disclosures,* defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal, or most advantageous, market for the asset or liability in an orderly transaction between market participants at the measurement date. The Fair Values Measurements Topic establishes a three-level fair value hierarchy that prioritizes the inputs used to measure fair value. This hierarchy requires entities to maximize the use of observable inputs when possible. The three levels of inputs used to measure fair value are as follows:

> Level 1: Unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities
>
> Level 2: Quoted prices in markets that are not considered to be active or financial instruments for which all significant inputs are observable, either directly or indirectly.
>
> Level 3: Prices or valuations that require inputs that are both significant to the fair value measure and unobservable.

A financial instrument's level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement.

The carrying amounts of the Cooperative's cash and cash equivalents, other receivables, investments, inventories, other assets, trade accounts payable, accrued expenses and liabilities, and other liabilities approximate fair value due to their short maturity. Investments in associated organizations are not considered a financial instrument because they represent nontransferable interests in associated organizations. Other assets and liabilities are not considered financial instruments because they represent activities specifically related to the Cooperative. Long term debt can not be traded in the market, and is specifically for electric cooperatives and, therefore, a value other than its outstanding principal cannot be determined.

The Cooperative may, and also does, invest idle funds in local banks money market accounts and CD's. The inputs used to measure idle funds are Level 1 measurements, as these funds are exchange traded funds in an active market.

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

Utility Plant Telecommunications and video plant are stated at original cost, which is the cost when first dedicated to public service. Such amount includes applicable supervisory and overhead cost including any construction period interest and taxes. Interest capitalized during the year was $119,796 for 2014 and $74,084 for 2013.

The cost of maintenance and repairs, including renewals of minor items of property, is charged to operating expenses. The cost of replacement of depreciable property units, as distinguished from minor items, is charged to plant. The units of property replaced or retired, including cost of removal, net of any salvage value, is charged to accumulated depreciation.

Notes to Financial Statements, continued

Note 1 Summary of Significant Accounting Policies, continued

The major classification of plant in service is:

	2014	2013
General support	$13,034,207	$12,682,671
Central office switching	2,493,900	2,394,945
Central office transmission	23,958,434	23,117,110
Cable and wire facilities	77,930,751	77,581,460
General plant	3,453	3,453
Subtotal telecommunications plant	117,420,745	115,779,639
Headend equipment	4,836,565	4,736,195
Other video plant	1,480,013	876,518
Subtotal video plant	6,316,578	5,612,713
	$123,737,323	$121,392,352

Depreciation Provision has been made for depreciation on the basis of estimated lives of assets, using the straight-line method. Rates are as follows:

	Foothills	Cellular
General support	2.7% - 15.8%	
Central office switching and headend	7.5%	5.0%
Central office transmission	11.9%	
Cable and wire facilities	5.1% - 9.4%	5.1% - 6.6%

Advertising Advertising costs are expensed as incurred.

Income Taxes The Cooperative is exempt from federal and state income taxes under IRS Code Section 501(c)(12). Certain unrelated business activities are subject to federal income taxes. Cellular Services is a "C" corporation for federal and state income tax purposes.

The Cooperative's accounting policy provides that a tax expense/benefit from an uncertain tax position may be recognized when it is more likely than not that the position will be sustained upon examination, including resolutions of any related appeals or litigation processes, based on the technical merits. Management believes the Cooperative has no uncertain tax positions resulting in an accrual of tax expense or benefit. The Cooperative recognizes interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expenses. The Cooperative did not recognize any interest or penalties during the years ended December 31, 2014 and 2013. The Cooperative's income tax return is subject to possible examination by taxing authorities until the expiration of related statues of limitations on the return, which is generally three years.

Comprehensive Income Comprehensive income includes both net margin and other comprehensive income. Other comprehensive income represents the change in funded status of the accumulated postretirement benefit obligation.

Notes to Financial Statements, continued

Note 1 Summary of Significant Accounting Policies, continued

Subsequent Events Management has evaluated subsequent events through March 3, 2015, the date the financial statements were available to be issued. There were no significant subsequent events to report.

Note 2 Investments

Cellular Services is a partner in East Kentucky Network, LLC (EKN). EKN provides cellular service, fiber connections, paging, and other services in eastern Kentucky. EKN is comprised of Cellular Services and four (4) other independent telephone companies. The investment is accounted for using the equity method of accounting and includes capital investments.

Note 3 Non Regulated Activities

Deregulated customer premises equipment is stated at cost; material held for lease or resale is stated at average cost. CPE also includes inside wire revenues and expenses. Depreciation is provided on a straight-line basis at 11.9% per year.

The Cooperative provides long distance telephone service under the name of Foothills Long Distance (FLD). FLD revenues are billed and collected through Foothills Telephone. A monthly fee is recorded based on telephone usage. FLD purchases minutes of long distance to resell to its customers from an unrelated party.

Non regulated investments also include amounts that the Cooperative has invested to provide internet services to its customers. The Cooperative pays an unrelated party for the help desk and access to the internet system.

The following is a summary of non-regulated activities:

	Income	Expenses	Net
Customer premises equipment	$235,719	$226,262	$9,457
Internet activities	4,152,680	3,543,560	609,120
Long distance services	421,536	342,204	79,332
Fiber to the home video	4,190,557	4,722,005	(531,448)
Total - 2014	$9,000,492	$8,834,031	$166,461

	Income	Expenses	Net
Customer premises equipment	$248,882	$266,131	($17,249)
Internet activities	3,953,629	2,707,707	1,245,922
Long distance services	418,616	361,505	57,111
Fiber to the home video	3,900,935	3,887,907	13,028
Total - 2013	$8,522,062	$7,223,250	$1,298,812

Note 4 Long Term Debt

All telecommunications assets, except motor vehicles, are pledged as collateral on the long term debt due RUS, Rural Telephone Bank ("RTB") and National Bank for Cooperatives ("CoBank"). During 2012 the long term debt payable to RUS and RTB was refinanced with proceeds from CoBank and are included with the debt due from CoBank.

Note 4 Long Term Debt, continued

Long term debt is as follows:

	2014	2013
RUS, Broadband, 2.43% - 3.33%	$4,236,689	$2,896,855
CoBank, 6.25%	11,110,895	15,106,053
	15,347,584	18,002,908
Less current portion	4,100,000	4,100,000
Long term portion	$11,247,584	$13,902,908

Principal payments for the next five years are as follows: 2015 - $4,100,000; 2016 - $4,100,000; 2017 - $4,100,000; 2018 - $3,250,000; 2019 - $170,000.

Note 5 Patronage Capital

The long term debt agreement contains restrictions on the return to patrons of capital contributed by them. The restrictions relate in general to the Cooperative's net worth and assets, as defined. The net worth of the Cooperative at December 31, 2014, was 80%. Patronage capital consisted of:

	2014	2013
Assigned to date	$83,676,787	$78,267,466
Assignable margins	5,513,402	7,039,887
Unassigned nonoperating margins	21,090,733	19,445,293
Patronage capital unlocated	1,079,800	1,097,226
Retirements to date	(26,493,781)	(25,208,625)
Total	$84,866,941	$80,641,247

Note 6 Pension Plan

All eligible employees of the Cooperative participate in the NTCA Retirement and Security 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. A unique characteristic of a multiemployer plan compared to a single employer plan is that all plan assets are available to pay benefits of any plan participant. 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.

The Cooperative's contributions to the R&S Plan in 2014 and 2013 represent less than 5 percent of the total contributions made to the plan by all participating employers. The Cooperative made contributions to the plan of $543,790 in 2014 and $512,926 in 2013. There have been no significant changes that affect the comparability of 2014 and 2013.

Note 6 Pension Plan, continued

In the R&S Plan, a "zone status" determination is not required, and therefore not determined, under the Pension Protection Act ("PPA") of 2006. In addition, the accumulated benefit obligations and plan assets are not determined or allocated separately by individual employer. In total, the R&S Plan was between 88 percent and 80 percent funded at January 1, 2014 and 2013 based on the PPA funding target and PPA actuarial value of assets on those dates. Because the provisions of the PPA do not apply to the R&S Plan, funding improvement plans and surcharges are not applicable. Future contribution requirements are determined each year as part of the actuarial valuation of the plan and may change as a result of plan experience.

Note 7 Accumulated Postretirement Benefits

The Cooperative sponsors a defined benefit plan that provides medical insurance coverage to retirees and their dependents until they reach age 65. Participating retirees and dependents do not contribute to the projected cost of coverage. Employees qualify with a minimum age of 55 and meeting the Rule of 85.

The funded status of the plan was as follows:

	2014	2013
Projected benefit obligation	($6,897,963)	($6,506,273)
Plan assets at fair value	2,832,179	2,487,258
Total	($4,065,784)	($4,019,015)

The components of net periodic postretirement benefit costs are as follows:

	2014	2013
Benefit obligation at beginning of year	$4,019,015	$3,960,977
Components of net periodic benefit cost:		
Service cost	192,979	191,948
Interest cost	335,106	318,210
Expected return on assets	(198,253)	(180,326)
Net periodic benefit cost	329,832	329,832
Benefits paid	(283,063)	(271,794)
Accumulated other comprehensive accounting	-	-
Benefit obligation at end of year	$4,065,784	$4,019,015

For measurement purposes, an 8.5% annual rate of increase, decreasing by 0.5% per year until 5.5% per year, in the per capita cost of covered health care benefits was assumed. The discount rate used in determining the accumulated benefit obligation was 5.5% for 2014 and 2013.

The projected retiree benefit payments are expected to be as follows: 2015 - $281,000; 2016 - $272,000; 2017 – $268,000; 2018 - $267,000; 2019 - $270,000.

Note 8 Risk Management

The Cooperative is exposed to various forms of losses of assets associated with, but not limited to, fire, personal liability, theft, vehicular accidents, errors and omissions, fiduciary responsibility, workers compensation, etc. Each of these areas is covered through the purchase of commercial insurance.

Notes to Financial Statements, continued

Note 9 Commitments

The Cooperative has various agreements outstanding with local contractors. Under these agreements, the contractors will perform certain construction, maintenance, and other work at specified hourly rates or unit cost, or on an as needed basis. The duration of these contracts are one to three years.

Note 10 Significant Event

The Cooperative was awarded a Broadband Initiatives Program ("BIP") Grant from the United States of America through the Department of Agriculture, Rural Utilities Service ("RUS"). The project would provide broadband internet service to the counties served in southeastern Kentucky. The total project cost is $21,818,512, of which $14,680,738 is in the form of a grant. The remaining funds must be secured with RUS debt and general funds. The Cooperative started the project during 2012. The Grant requires that the project be completed within three (3) years from the date of the Grant, however, RUS has granted an extension on the project until September 30, 2015.

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Foothills Rural Telephone Cooperative Corporation and Subsidiary

Consolidating Balance Sheet, December 31, 2014

Assets	Foothills Telephone	Cellular Services	Eliminations	Consolidated
Current Assets:				
Cash and cash equivalents	$13,964,352	$2,208,800		$16,173,152
Accounts receivable, less allowance for 2014 of $53,096	681,716			681,716
Other accounts receivable	1,599,544		(68,269)	1,531,275
Materials and supplies, at average cost	1,213,807			1,213,807
Prepayments	559,296			559,296
	18,018,715	2,208,800	(68,269)	20,159,246
Other Assets:				
Investment securities available for sale	4,960,642	100,000		5,060,642
Investment in associated organization	26,507,364	20,864,241	(26,507,364)	20,864,241
Nonregulated investments	1,811,009			1,811,009
	33,279,015	20,964,241	(26,507,364)	27,735,892
Telecommunications Plant, at original cost:				
In service	117,420,745	6,316,578		123,737,323
Under construction	6,776,300	8,330		6,784,630
	124,197,045	6,324,908		130,521,953
Less accumulated depreciation	69,973,411	2,929,030		72,902,441
	54,223,634	3,395,878		57,619,512
Total	$105,521,364	$26,568,919	($26,575,633)	$105,514,650
Liabilities and Member's Equities				
Current Liabilities:				
Accounts payable	$1,237,218	$68,269	($68,269)	$1,237,218
Current portion of long term debt	4,100,000			4,100,000
Customer deposits	207,506			207,506
Other current and accrued expenses	1,520,959			1,520,959
	7,065,683	68,269	(68,269)	7,065,683
Long Term Debt	11,247,584			11,247,584
Accrued Postretirement Benefits	4,065,784			4,065,784
Members' Equities:				
Memberships and capital investment	628,314	8,257,826	(8,257,826)	628,314
Patronage capital and retained earnings	84,873,655	18,242,824	(18,249,538)	84,866,941
Donated capital	124,537			124,537
Accum other comprehensive income	(2,484,193)			(2,484,193)
	83,142,313	26,500,650	(26,507,364)	83,135,599
Total	$105,521,364	$26,568,919	($26,575,633)	$105,514,650

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

Consolidating Statement of Revenue and Comprehensive Income
for the year ended December 31, 2014

	Foothills Telephone	Cellular Services	Eliminations	Consolidated
Operating Revenue:				
Basic local network services	$6,293,692	$225,933	($69,009)	$6,450,616
Network access services	14,721,980			14,721,980
Billing and collection	482,228			482,228
Miscellaneous	902,826			902,826
Less provision for uncollectibles	(74,000)			(74,000)
	22,326,726	225,933	(69,009)	22,483,650
Operating Expenses:				
Plant specific operations	4,902,815	440,469	(69,009)	5,274,275
Plant nonspecific operations	2,037,639	1,001		2,038,640
Depreciation	5,320,522	406,283		5,726,805
Customer operations	1,711,586	5,815		1,717,401
Corporate operations	1,607,563	21,445		1,629,008
Taxes	1,216,451	163,905		1,380,356
	16,796,576	1,038,918	(69,009)	17,766,485
Operating margins	5,530,150	(812,985)		4,717,165
Nonoperating Margins				
Other nonoperating income	442,627	1,072,623	(259,638)	1,255,612
Non regulated activities	166,461			166,461
	609,088	1,072,623	(259,638)	1,422,073
Margins before interest charges	6,139,238	259,638	(259,638)	6,139,238
Interest Charges:				
Interest on long-term debt	615,659			615,659
Other	10,177			10,177
	625,836			625,836
Net Margins	5,513,402	259,638	(259,638)	5,513,402
Other Comprehensive Income:				
Accumulated postretirement benefits	150,168			150,168
Net Comprehensive Income	$5,663,570	$259,638	($259,638)	$5,663,570

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

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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*

To the Board of Directors
Foothills Rural Telephone Cooperative

I 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 financial statements of Foothills Rural Telephone Cooperative, which comprise the balance sheets as of December 31, 2014 and 2013, and the related statements of revenue and comprehensive income, members' equities and cash flows for the years then ended, and related notes to the financial statements, and have issued my report thereon dated March 3, 2015. My report includes a reference to other auditors who audited the financial statements of East Kentucky Network, LLC, as described in my report on Foothills Rural Telephone's financial statements. This report does not include the results of the other auditor's testing of internal control over financial reporting or compliance and other matters that are reported on separately by those auditors.

Internal Control Over Financial Reporting

In planning and performing my audit of the financial statements, I considered Foothills Rural Telephone's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing my opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Foothills Rural Telephone's internal control. Accordingly, we do not express an opinion on the effectiveness of Foothills Rural Telephone'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.

My 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 my audit I did not identify any deficiencies in internal control that I 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 Foothills Rural Telephone's financial statements are free of material misstatement, I performed test 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 my audit, and accordingly, I do not express such an opinion. The results of my 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 my testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the organization'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 organization's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Alan M. Zumstein

Alan M. Zumstein, CPA
March 3, 2015

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Independent Auditor's Report on Compliance with Aspects of Contractual Agreements and Regulatory Requirements for Telephone Borrowers

Board of Directors
Foothills Rural Telephone Cooperative

Independent Auditor's Report

I 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 financial statements of Foothills Rural Telephone Cooperative ("the Cooperative"), which comprise the balance sheet as of December 31, 2014, and the related statements of revenue and comprehensive income, patronage capital, and changes in cash flows for the year then ended, and the related notes to the financial statements, and have issued my report thereon dated March 3, 2015. In accordance with *Government Auditing Standards*, we have also issued my report dated March 3, 2015, on my consideration of the Cooperative's internal control over financial reporting and on my 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 related to my audit have been furnished to management.

In connection with my audit, nothing came to my attention that caused me to believe that the Cooperative 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 and clarified in the RUS policy memorandum dated February 7, 2014, insofar as they relate to accounting matters as enumerated below. However, my audit was not directed primarily toward obtaining knowledge of noncompliance. Accordingly, had I performed additional procedures, other matters may have come to my attention regarding the Cooperative'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 my audit, I noted no matters regarding the Cooperative's accounting and records to indicate that the Cooperative 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;

Board of Directors
Foothills Rural Telephone Cooperative - 2

- 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 material and supplies;
- Prepare accurate and timely Financial and Operating Reports;
- Obtain written approval of the RUS to enter into any contract, agreement, or lease with an affiliate as defined in Part 1773 (e)(2)(i);
- Disclose material related party transactions in the financial statements, in accordance with requirements for related parties in generally accepted accounting principles, and;
- Comply with the requirements for the detailed schedule of investments, which are listed below.

Foothills Telephone formed a wholly-owned subsidiary, Cellular Services, LLC, which communications and video service and also is a one-fifth (1/5) owner of a limited liability company that provides cellular and other communications services. The initial investment was $820,000. The investment is comprised of the following:

	Investment	Profits
Balance, beginning of year	$8,257,826	$17,983,186
Activity for 2014		266,352
Balance, end of year	$8,257,826	$18,249,538

This report is intended solely for the information and use of the board of directors, management, 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 distributions is not limited.

Alan Zumstein

Alan M. Zumstein, CPA
March 3, 2015