

**MOUNTAIN RURAL TELEPHONE COOPERATIVE
AND SUBSIDIARY
KY 506**

FINANCIAL REPORT

DECEMBER 31, 2020

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Jones, Nale & Mattingly PLC

INDEPENDENT AUDITOR'S REPORT

Board of Directors
Mountain Rural Telephone Cooperative and Subsidiary
West Liberty, Kentucky

We have audited the accompanying consolidated financial statements of Mountain Rural Telephone Cooperative and Subsidiary (the Cooperative), which comprise the consolidated balance sheets as of December 31, 2020 and 2019, and the related consolidated statements of income and comprehensive income, changes in members' equities, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

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

Auditor's Responsibility

Our responsibility is to express an opinion 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the 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 opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mountain Rural Telephone Cooperative and Subsidiary as of December 31, 2020 and 2019, and the results of their operations and their cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Correction of Errors

As described in Note 16 to the financial statements, the Cooperative discovered errors in the amounts previously reported for accrued income taxes and income tax expense, and accumulated postretirement benefits and accumulated postretirement expense. Accordingly, amounts presented for accrued income taxes and income tax expense, and accrued postretirement benefits and accumulated postretirement expense have been restated in the 2019 financial statements now presented, and a cumulative effect adjustment has been made to patronage capital as of January 1, 2019. Our opinion is not modified with respect to this matter.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated March 2, 2021, on our consideration of Mountain Rural Telephone Cooperative 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 the Cooperative's internal control over financial reporting and compliance.

Jones, Nale & Mattingly PLC

Louisville, Kentucky
March 2, 2021

MOUNTAIN RURAL TELEPHONE COOPERATIVE AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

December 31, 2020 and 2019

	<u>2020</u>	<u>2019</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 37,281,471	\$ 29,661,735
Accounts receivable, less allowance for doubtful accounts of \$52,207 in 2020 and \$10,709 in 2019	237,477	345,418
Other receivables	23	19,464
Materials and supplies, at average cost	1,153,997	970,552
Prepaid expenses	370,706	29,990
Total current assets	<u>39,043,674</u>	<u>31,027,159</u>
NON-CURRENT ASSETS		
Investment securities	12,805,931	13,655,443
Associated organizations	32,338,539	33,530,670
Pension plan prefunding	2,335,847	2,408,243
Nonregulated property	3,368,518	3,313,801
Total non-current assets	<u>50,848,835</u>	<u>52,908,157</u>
PROPERTY AND EQUIPMENT		
In service	135,669,963	133,430,237
Under construction	2,832,279	1,489,769
	<u>138,502,242</u>	<u>134,920,006</u>
Less accumulated depreciation	87,708,670	83,655,386
	<u>50,793,572</u>	<u>51,264,620</u>
	<u>\$ 140,686,081</u>	<u>\$ 135,199,936</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

	<u>2020</u>	<u>2019</u>
LIABILITIES AND MEMBERS' EQUITIES		
CURRENT LIABILITIES		
Current portion of long-term debt	\$ 404,936	\$ 395,488
Accounts payable	616,732	903,488
Customer deposits	260,694	211,235
Accrued income taxes	--	130,988
Accrued leave	2,204,488	1,990,942
Accrued expenses	120,661	376,130
Total current liabilities	<u>3,607,511</u>	<u>4,008,271</u>
NON-CURRENT LIABILITIES		
Long-term debt, less current portion	5,367,105	5,772,056
Accumulated postretirement benefits	4,109,527	3,441,437
Deferred tax liabilities	2,770,000	2,870,000
Total non-current liabilities	<u>12,246,632</u>	<u>12,083,493</u>
MEMBERS' EQUITIES		
Memberships and capital investments	137,116	130,360
Patronage capital and retained earnings	132,328,630	125,949,642
Donated capital	1,323,975	1,323,975
Accumulated comprehensive income (loss)	(8,957,783)	(8,295,805)
Total members' equities	<u>124,831,938</u>	<u>119,108,172</u>
	<u>\$ 140,686,081</u>	<u>\$ 135,199,936</u>

MOUNTAIN RURAL TELEPHONE COOPERATIVE AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
Years Ended December 31, 2020 and 2019

	2020	2019
Operating revenues:		
Local network service	\$ 6,649,809	\$ 6,491,082
Network access service	10,757,151	11,636,935
Carrier billing and collection	335,155	253,175
Miscellaneous	505,804	649,456
Access revenue	7,000	44,000
Total operating revenues	18,254,919	19,074,648
Operating expenses:		
Plant specific operations expense	3,467,409	3,456,546
Plant non-specific	2,082,864	1,688,171
Depreciation	4,793,602	5,815,013
Customer operations expense	1,395,414	1,351,495
Corporate operation expense	1,954,097	2,025,755
Other deductions	111,535	126,743
Other taxes	882,274	923,568
Total operating expenses	14,687,195	15,387,291
Operating income	3,567,724	3,687,357
Other income (expense):		
Interest income	455,922	553,146
Interest expense	(141,269)	(150,465)
Other income	1,422,227	456,238
Income in limited liability company	2,172,411	4,787,430
Total other income (expense)	3,909,291	5,646,349
Income before income taxes	7,477,015	9,333,706
Income tax (expense)	(642,516)	(1,349,965)
Net income before nonregulated income	6,834,499	7,983,741
Nonregulated income	2,461,485	1,759,595
Net income	\$ 9,295,984	\$ 9,743,336
Other comprehensive income (loss)		
Accumulated postretirement expense	(661,978)	(4,742,919)
Total comprehensive income	\$ 8,634,006	\$ 5,000,417

The Notes to Consolidated Financial Statements are an integral part of these statements.

MOUNTAIN RURAL TELEPHONE COOPERATIVE AND SUBSIDIARY

STATEMENTS OF CHANGES IN MEMBERS' EQUITIES
Years Ended December 31, 2020 and 2019

	<u>Memberships</u>	<u>Patronage Capital</u>	<u>Other Equity</u>	<u>Accumulated Other Comprehensive (Loss)</u>	<u>Total</u>
Balance, January 1, 2019, as previously reported	\$ 129,469	\$ 115,816,635	\$ 1,323,802	\$ (3,552,886)	\$ 113,717,020
Prior period adjustment	--	2,893,595	--	--	2,893,595
Balance, January 1, 2019, as restated	<u>129,469</u>	<u>118,710,230</u>	<u>1,323,802</u>	<u>(3,552,886)</u>	<u>116,610,615</u>
Net income	--	9,743,336	--	--	9,743,336
Postretirement benefit obligations					
Amortization	--	--	--	414,074	414,074
Adjustments	--	--	--	(5,156,993)	(5,156,993)
Refunds of capital credits	--	(2,503,924)	--	--	(2,503,924)
Memberships issued, net	891	--	--	--	891
Other equities	--	--	173	--	173
Balance, December 31, 2019	<u>130,360</u>	<u>125,949,642</u>	<u>1,323,975</u>	<u>(8,295,805)</u>	<u>119,108,172</u>
Net income	--	9,295,984	--	--	9,295,984
Postretirement benefit obligations					
Amortization	--	--	--	440,585	440,585
Adjustments	--	--	--	(1,102,563)	(1,102,563)
Refunds of capital credits	--	(2,916,996)	--	--	(2,916,996)
Memberships issued, net	6,756	--	--	--	6,756
Balance at December 31, 2020	<u>\$ 137,116</u>	<u>\$ 132,328,630</u>	<u>\$ 1,323,975</u>	<u>\$ (8,957,783)</u>	<u>\$ 124,831,938</u>

The Notes to Consolidated Financial Statements are an integral part of these statements.

MOUNTAIN RURAL TELEPHONE COOPERATIVE AND SUBSIDIARY

STATEMENTS OF CASH FLOWS
Years Ended December 31, 2020 and 2019

	<u>2020</u>	<u>2019</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income	\$ 9,295,984	\$ 9,743,336
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	4,793,602	5,815,013
Forgiveness of debt	(1,311,402)	--
Net loss (income) in associated organization	(2,172,411)	(4,787,430)
Change in assets and liabilities, net of the effects of investing and financing activities:		
Accounts receivable	107,941	(27,518)
Other receivables	19,441	(19,464)
Material and supplies	(183,445)	617,350
Prepaid expenses	(340,716)	(3,531)
Accounts payable	(286,756)	(485,172)
Customer deposits	49,459	7,024
Accrued expenses	(172,911)	1,780,686
Deferred tax liabilities	(100,000)	270,000
Net cash provided by operating activities	<u>9,698,786</u>	<u>12,910,294</u>
 CASH FLOWS FROM INVESTING ACTIVITIES		
Plant additions	(4,316,442)	(2,082,106)
Purchases of securities	--	(628,422)
Sales of securities	849,512	--
Associated organizations	3,364,542	1,729,799
Nonregulated property	(54,717)	(80,764)
Net cash provided by (used in) investing activities	<u>(157,105)</u>	<u>(1,061,493)</u>
 CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on long-term debt	(395,503)	(386,306)
Proceeds from long-term debt	1,311,402	--
Prefund pension plan	72,396	(161,075)
Membership and capital investments	6,756	891
Retirements of capital credits	(2,916,996)	(2,503,924)
Increase in donated capital	--	173
Net cash (used in) financing activities	<u>(1,921,945)</u>	<u>(3,050,241)</u>
 Net increase in cash and cash equivalents	7,619,736	8,798,560
 Cash and cash equivalents:		
Beginning of year	<u>29,661,735</u>	<u>20,863,175</u>
End of year	<u>\$ 37,281,471</u>	<u>\$ 29,661,735</u>
 SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Interest on long term debt	\$ 141,269	\$ 150,465
Income taxes paid	1,220,958	--

The Notes to Consolidated Financial Statements are an integral part of these statements.

MOUNTAIN RURAL TELEPHONE COOPERATIVE AND SUBSIDIARY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies

Mountain Rural Telephone Cooperative Corporation (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. The significant policies are as follows:

Principles of Consolidation

The consolidated financial statements include the accounts of the Cooperative and its wholly owned Subsidiary, Mountain Telecommunications, Inc. (Mountain Telecommunications). All significant inter-company accounts and transactions have been eliminated.

Nature of Business

The Cooperative has completed construction allowing it to expand its 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 is also able to provide high speed internet, virtual private networks, and voice over internet protocol (VoIP). This is accomplished through Fiber to the Home (FTTH) technology.

Estimates

The preparation of financial statements in accordance 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.

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. For purposes of the statement of cash flows, the Cooperative considers temporary investments having original maturities of three months or less to be cash equivalents. The Cooperative maintains its cash balances, which may exceed the federally insured limit, with several financial institutions. Management believes that credit risk related to the accounts is minimal.

Investment Securities

Investment securities consist of certificates of deposit and bank repurchase agreements in local banks and are carried at cost, which approximates fair value, and are held to maturity. Fair value is determined by quoted prices for similar certificates of deposit in active markets (Level 2) as defined under U.S GAAP.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies (Continued)

Accounts Receivable

Accounts receivable are stated at net realizable value. The allowance for doubtful 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 ten percent of outstanding accounts receivable at December 31, 2020 and 2019. The number of access lines was 12,395 for 2020 and 12,713 at 2019.

Materials and Supplies

Materials and supplies are composed primarily of telephone material and supplies used in the telecommunications plant. The inventory is valued at the lower of cost or net realizable value, cost being determined by the average cost method.

Telecommunications Revenue Recognition

Revenues are recognized when earned. Bills are sent to customers on credit the first of each month with local service being billed a month in advance of service. Sales are concentrated in a portion of five (5) southeastern Kentucky counties. Payments are due 10 days from the date of billing. If payment has not been made, then customers are subject to disconnect on the 21st day of the month.

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

Video revenue is recognized when earned regardless of the period in which they are billed. Programming transmission is purchased from networks at various amounts based on the number of customers receiving the service.

Taxes

The Cooperative's policy is to exclude sales tax from revenue when collected and expenses when paid and instead, record collection and payment of sales taxes through a liability account.

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.

Advertising

Advertising costs are expensed as incurred. For the years ended December 31, 2020 and 2019, these costs were \$70,462 and \$89,119, respectively.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies (Continued)

Telecommunications Plant

Telecommunications plant is 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 \$26,200 for 2020 and \$43,081 for 2019.

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.

Provision has been made for depreciation on the basis of estimated lives of assets (as prescribed by the Public Service Commission of Kentucky) using the straight-line method. Rates are as follows:

	<u>Telephone</u>	<u>Telecom</u>
General support	2.7% - 15.8%	20.0%
Central office switching	7.5%	
Central office transmission	11.0%	
Cable wire facilities	2.2% - 9.4%	

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. Mountain Telecommunications is a "C" corporation that pays income taxes on its net income. Income taxes are provided for the tax effects of transactions reported in the financial statements and consist of taxes currently due plus deferred taxes related primarily to differences between the basis of investments in associated organizations. The deferred tax assets and liabilities represent future tax return consequences of those differences, which will either be taxable or deductible when the assets or liabilities are recovered or settled.

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, 2020 and 2019.

The Cooperative's income tax return is subject to possible examination by taxing authorities until the expiration of related statutes of limitations on the return, which is generally three years for federal and four years for state.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1. Summary of Significant Accounting Policies (Continued)

Comprehensive Income

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

Subsequent Events

Management has evaluated subsequent events through March 2, 2021, the date the consolidated financial statements were available to be issued.

Reclassifications

Certain amounts presented in the 2019 financial statements have been reclassified to conform with the 2020 presentation.

Recently issued accounting pronouncements

In February 2016, the FASB issued ASU No. 2016-02, *Leases*. The standard requires all leases with lease terms over 12 months to be capitalized as a right-of-use asset and lease liability on the balance sheets at the date of lease commencement. Leases will be classified as either finance or operating. This distinction will be relevant for the pattern of expense recognition in the statements of income. This standard will be effective for the year ending December 31, 2022.

In June 2016, the FASB issued ASU No. 2016-13 (ASU 2016-13), *Financial Instruments – Credit Losses*. This guidance replaces the incurred loss model with an expected loss model, which is referred to as the current expected credit loss (CECL) model. The CECL model is applicable to the measurement of credit losses on financial assets measured at amortized cost, including loan and financing receivables, held-to-maturity debt securities and reinsurance receivables. It also applies to off-balance sheet credit exposures not accounted for as insurance (loan commitments, standby letters of credit, financial guarantees, and other similar instruments) and net investments in leases recognized by a lessor. This standard is effective for the year ending December 31, 2023.

Management is currently in the process of evaluating the impact of the adoption of these ASU's on the Cooperative's financial statements.

Note 2. Fair Value Measurements

U.S. GAAP provides a framework for fair value measurements. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The methodology for measuring fair value specifies a three-tier hierarchy of valuation techniques based upon whether the inputs to those valuation techniques are based on quoted prices of identical assets or liabilities (Level 1), significant other observable inputs (Level 2), or significant other unobservable inputs that reflect a company's own assumptions of market participant valuation (Level 3).

The Cooperative invests idle funds with local banks in certificates of deposits and U.S. Treasury Notes.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 2. Fair Value Measurements (Continued)

The Cooperative's investment securities measured at fair value on a non-recurring basis are as follows:

	<u>Fair value</u>	<u>Fair value measurements using:</u>	
		<u>Unadjusted quoted prices (Level 1)</u>	<u>Significant other observable inputs (Level 2)</u>
<u>December 31, 2020</u>			
Certificates of deposit	\$ 3,000,000	\$ --	\$ 3,000,000
Bank repurchase agreements	9,805,931	9,805,931	--
	<u>\$ 12,805,931</u>	<u>\$ 9,805,931</u>	<u>\$ 3,000,000</u>
<u>December 31, 2019</u>			
Certificates of deposit	\$ 3,000,000	\$ --	\$ 3,000,000
Bank repurchase agreements	10,655,443	10,655,443	--
	<u>\$ 13,655,443</u>	<u>\$ 10,655,443</u>	<u>\$ 3,000,000</u>

Note 3. Associated Organizations

The amounts for East Kentucky Network, LLC ("EKN") represents Mountain Telecommunications' investment in a limited liability company with other telephone companies in eastern Kentucky for the purpose of providing cellular telephone, and other services. The investment is accounted for using the equity method since Mountain Telecommunications is a 20% member and has the ability to significantly influence EKN's operations and financial policies. EKN has been paying distributions of approximately 50% of the income allocated in cash during the following year. The following is summarized financial information of EKN as of and for the years ended December 31, 2020 and 2019:

	<u>2020</u>	<u>2019</u>
Assets	<u>\$ 213,440,853</u>	<u>\$ 200,788,162</u>
Liabilities	<u>\$ 51,748,153</u>	<u>\$ 33,134,801</u>
Equity	<u>\$ 161,692,700</u>	<u>\$ 167,653,361</u>
Revenues and other income	<u>\$ 131,986,587</u>	<u>\$ 132,935,842</u>
Expenses and other expenses	<u>\$ 120,802,140</u>	<u>\$ 118,866,602</u>
Net income	<u>\$ 11,184,447</u>	<u>\$ 14,069,240</u>

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 4. Telecommunications Plant

The major classification of plant service is:

	2020	2019
Telecommunications Plant:		
General support	\$ 16,215,762	\$ 16,370,615
Central office switching	1,601,629	1,590,117
Central office transmission	27,710,315	26,772,760
Cable wire facilities	90,136,823	88,691,311
Intangibles	2,434	2,434
	135,666,963	133,427,237
Telecom Plant:		
General support	3,000	3,000
Total	\$ 135,669,963	\$ 133,430,237

Depreciation expense for the years ended December 31, 2020 and 2019 was \$4,793,602 and \$5,815,013, respectively.

Note 5. Nonregulated Activities

Deregulated customer premises equipment is stated at cost; material held for lease or resale is stated at average cost. Customer Premises Equipment (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 Mountain Telephone Long Distance ("MTLD"). MTLD revenues are billed and collected through the Cooperative. A monthly fee is recorded based on telephone usage. MTLD purchases minutes of long distance to resell to its customers from an unrelated party. Nonregulated investments also include amounts that the Cooperative has invested to provide internet services to its customers. The Cooperative has an in-house help desk service department and utilizes an answering service after hours for emergencies only. The following is a summary of nonregulated activities:

	2020	2019
Investments	\$ 454,338	\$ 448,679
Material and supplies	222,613	165,557
Plant assets	7,472,428	6,706,330
Reserve for depreciation	(4,780,861)	(4,006,765)
	\$ 3,368,518	\$ 3,313,801

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 5. Nonregulated Activities (Continued)

	Income	Expenses	Net
Customer premises equipment	\$ 1,008,873	\$ 2,148,243	\$ (1,139,370)
Internet activities	3,865,406	943,212	2,922,194
Long distance services	357,922	322,826	35,096
Video services	3,503,422	3,059,564	443,858
Security/Surveillance	524,030	324,323	199,707
Total - 2020	\$ 9,259,653	\$ 6,798,168	\$ 2,461,485
	Income	Expenses	Net
Customer premises equipment	\$ 760,340	\$ 1,932,702	\$ (1,172,362)
Internet activities	3,583,483	1,221,215	2,362,268
Long distance services	449,477	428,573	20,904
Video services	3,212,642	2,967,601	245,041
Security/Surveillance	685,760	382,016	303,744
Total - 2019	\$ 8,691,702	\$ 6,932,107	\$ 1,759,595

Note 6. Long-Term Debt

All telecommunications assets, except motor vehicles, are pledged as collateral on the long-term debt due to the U.S. Department of Agriculture, Rural Development (“USDA”). The debt was incurred for the FSN project as described earlier and is due in monthly installments of varying amounts. Long-term debt is as follows:

	2020	2019
RUS Broadband Loan		
2.27%-2.46%	\$ 5,772,041	\$ 6,167,544
Less current portion	404,936	395,488
Long-term portion	\$ 5,367,105	\$ 5,772,056

Principal payments for the next five years and thereafter are as follows:

2021	\$ 404,936
2022	414,596
2023	424,486
2024	434,599
2025	444,980
Thereafter	3,648,444
	\$ 5,772,041

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 7. 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, 2020 and 2019 was 94% and 93%, respectively. Patronage capital consists of the following:

	2020	2019
Assigned	\$ 116,113,912	\$ 109,234,125
Assignable	9,295,984	9,743,336
Unassigned	54,473,726	51,307,086
Retirements to date	(47,554,992)	(44,334,905)
Total	\$ 132,328,630	\$ 125,949,642

Note 8. Pension Plan

All eligible non-union employees of the Cooperative participate in the National Telephone Cooperative 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. 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. There have been no significant changes that affect the comparability of 2020 and 2019. The Cooperative uses a January 1, 2020 and January 1, 2019 measurement date for the plan.

The Cooperative's contributions to the R&S Plan in 2020 and 2019 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 \$426,540 in 2020 and \$433,560 in 2019.

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 over 100 and 105 percent funded at January 1, 2020 and 2019, respectively, 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.

The NTCA Board of Directors amended the 2018 R&S Program specifications at the recommendation of the Plan Trust Committee to include the following changes:

- Basic contribution rates will increase by 19%.
- The program's current surcharge will expire at the end of 2018, and a new surcharge contribution of 50% of the member's elected contribution rate will begin in 2019. This surcharge is expected to continue for approximately 12 years.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 8. Pension Plan (Continued)

- A prefunding option was added to allow members the option to prefund their future surcharge contributions in a single payment prior to the start of the new surcharge effective in 2019.
- Beginning January 1, 2018, for members that have adopted the Rule-of-85 (“ROE”) provision, the ROE charge will apply to both the member’s elected employer contribution rate and any required employee contribution rate.

Over the past several years, various actions have been taken to sustain the reserve of funds available to help meet the programs legally required minimum contribution amount. However, adverse economic conditions and regulatory changes have negatively affected all pension plans, including the R&S Program. Despite prudent decision-making by the program’s trust committee, the R&S Program’s minimum contribution amount is projected to exceed the current reserve and member contributions alone will not meet the minimum requirement. This expectation has led the program’s actuary to recommend the new surcharge contribution beginning in 2020. The R&S Program is offering prefunding to give members flexibility in addressing this situation at the Cooperative.

The prefunding contribution is expected to fund the member’s surcharge contribution for approximately 12 years.

- Each member’s prefunding contribution will be maintained in a notional account within the R&S Program and used to pay that member’s surcharge contributions.
- Each member’s prefunding account is maintained separately from other member’s prefunding accounts.
- Account funds will be invested with other R&S Program assets and grow at the same rate as the program’s overall investment returns.
- An annual statement will be provided to each member showing their specific prefunding account activity.

During 2016, the Cooperative prefunded the surcharge in an amount of \$2,326,221. This amount will be amortized over the 12-year period the surcharge is expected to continue.

Employees hired after January 1, 2016 are considered Schedule 2 employees. Contributions rates are as follows:

	2017 and after	2016 and before
Schedule 1 Employees		
Employer contributions	10.70%	8.30%
Employee contributions	4.00%	4.00%
Rate of 85 charges	5.50%	5.50%
Schedule 2 Employees		
Employer contributions	8.70%	6.30%
Employee contributions	6.00%	6.00%
Rate of 85 charges	5.50%	5.50%

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 9. Accumulated Postretirement Benefits

The Cooperative sponsors a defined benefit plan that provides medical insurance coverage to retirees and their dependents. Participating retirees and dependents do not contribute to the projected cost of coverage. Employees hired before January 1, 2016 (Schedule 1) qualify with a minimum age of 55 and meeting the Rule of 85. There have been no significant changes that affect the comparability of 2020 and 2019. The Cooperative uses a January 1, 2020 and January 1, 2019 measurement date for the plan.

The following illustrates the plan for those years ended December 31, 2020 and 2019:

	2020	2019
Benefit obligation, beginning of year	\$ 21,838,455	\$ 19,371,018
Service cost	751,448	602,748
Interest cost	969,842	925,577
Benefit payments	(571,068)	(534,273)
Actuarial loss	3,224,958	1,473,385
Benefit obligation, end of year	\$ 26,213,635	\$ 21,838,455
Fair value of plan assets, beginning of year	\$ 18,397,018	\$ 19,313,612
Actual return on plan assets	4,278,158	(382,321)
Benefit payments	(571,068)	(534,273)
Fair value of plan assets, end of year	\$ 22,104,108	\$ 18,397,018
Reconciliation of funded status:		
Funded status	\$ (4,109,527)	\$ (3,441,437)
Net amount recognized at year end	\$ (4,109,527)	\$ (3,441,437)
Amounts recognized in the balance sheet consists of:		
Noncurrent assets (liabilities)	\$ (4,109,527)	\$ (3,441,437)
Amounts included in accumulated other comprehensive income:		
Unrecognized actuarial gain (loss)	\$ (8,957,783)	\$ (8,295,805)
Components of net periodic benefit cost:		
Service cost	\$ 751,448	602,748
Interest cost	969,842	925,577
Expected return on plan assets	(1,547,288)	(1,287,791)
Amortization cost	440,585	414,074
Net periodic benefit cost	\$ 614,587	\$ 654,608

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 9. Accumulated Postretirement Benefits (Continued)

	2020	2019
Weight-average assumptions as of December 31:		
Discount rate	3.75%	4.30%
Expected return on plan assets	7.00%	7.00%
Rate of compensation increase	3.00%	3.00%
Effect of 1% trend sensitivity for medical plan:		
Projected benefit obligation	\$ 30,284,931	\$ 25,075,181
Net periodic benefit cost	\$ 1,281,733	\$ 1,202,690

The projected retiree benefit payments are expected to be as follows: 2021 - \$709,000; 2022 - \$736,000; 2023 - \$764,000; 2024 - \$793,000; 2025 - \$823,000.

The Plan's investments are reported at fair value as follows:

	Fair value	Fair value measurements using:	
		Unadjusted quoted prices (Level 1)	Significant other observable inputs (Level 2)
December 31, 2020			
US Equity	\$ 5,503,923	\$ 5,503,923	\$ --
International Equity	4,818,696	--	4,818,696
Low Volatility	3,426,137	--	3,426,137
High Yield	1,790,433	--	1,790,433
Real Estate	2,873,534	--	2,873,534
Investment Grade Fixed Income	3,249,304	--	3,249,304
Cash	442,081	442,081	--
	\$ 22,104,108	\$ 5,946,004	\$ 16,158,104
December 31, 2019			
US Equity	\$ 4,580,857	\$ 4,580,857	--
International Equity	4,010,550	--	4,010,550
Low Volatility	2,851,538	--	2,851,538
High Yield	1,490,158	--	1,490,158
Real Estate	2,391,612	--	2,391,612
Investment Grade Fixed Income	2,704,362	--	2,704,362
Cash	367,941	367,941	--
	\$ 18,397,018	\$ 4,948,798	\$ 13,448,220

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 10. Income Taxes

The components of income tax are as follows:

	December 31,	
	2020	2019
Current:		
Federal	\$ 550,506	\$ 844,362
State	192,010	235,603
	742,516	1,079,965
Deferred:		
Federal	(84,000)	216,000
State	(16,000)	54,000
	(100,000)	270,000
	\$ 642,516	\$ 1,349,965

The deferred tax liabilities in the accompanying balance sheets consist of the following components:

	December 31,	
	2020	2019
Deferred tax liabilities:		
Federal	\$ 2,327,000	\$ 2,296,000
State	443,000	574,000
	\$ 2,770,000	\$ 2,870,000

Note 11. 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 12. Contingencies

The Cooperative, occasionally, is involved in litigation arising in the normal course of business. While the results of such litigation cannot be predicted with certainty, management, based upon advice of counsel, believes that the final outcome will not have a material adverse effect on the financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 13. Revenue Recognition

Adoption of accounting pronouncement

The Cooperative adopted ASU 2014-09, *Revenue from Contracts with Customers* as of January 1, 2019 using a modified retrospective method. The new standard replaces existing revenue recognition rules with a single comprehensive model to use in accounting for revenue arising from contracts with customers. The adoption of ASU 2014-09 had no material impact on earnings or equity of the Cooperative.

Under ASU 2014-09, the timing of recognition of revenue for each performance obligation may differ from the timing of the customer billing, creating a contract asset or contract liability. Short-term contract liabilities are classified as customer deposits. The Cooperative has no contract assets or long-term contract liabilities.

Nature of goods and services

The following is a description of principal activities from which the Cooperative generates its revenues.

Telecommunications revenues – The Cooperative’s regulated sources of revenue are local network services, network access services (interstate and intrastate/interlata), carrier billing, broadband only and other service charges. The Cooperative’s nonregulated sources of revenue are customer premises and equipment, internet activities, long distance services, video services, and security/surveillance/bus systems.

Significant judgments

Revenues from sales of equipment are recognized when control has transferred to the customer. Telecommunication service revenues are recognized as the related service is provided. Services are deemed to be highly interrelated when the method and timing of transfer and performance risk are the same. Highly interrelated services that are determined to not be distinct have been grouped into a single performance obligation. Each month of services promised is a performance obligation. The series of monthly service performance obligations promised over the course of the contract are combined into a single performance obligation for purposes of the allocation.

The Cooperative has made judgments regarding transaction price, including but not limited to issues relating to variable consideration, time value of money and returns. When determined to be significant in the context of the contract, these items are considered in the valuation of transaction price at contract inception or modification, as appropriate.

Multiple performance obligations

The Cooperative sells bundled service and equipment offerings. In these instances, the Cooperative recognizes its revenue based on the relative standalone selling prices for each distinct service or equipment performance obligation or bundles thereof. The Cooperative estimates the standalone selling price of the device or accessory to be its retail price excluding discounts. The Cooperative estimates the standalone selling price of telecommunication service to be the price offered to customers on month-to-month contracts.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 13. Revenue Recognition

From time to time, the Cooperative may offer certain promotions to incentivize customers to switch to, or to purchase additional services from the Cooperative. Under these types of promotions, an eligible customer may receive an incentive in the form of a discount off additional services purchased shown as a rebate or credit to the customer's monthly bill. Rebates are amortized over the life of the contract and are recognized when included in the customer's monthly bill.

Disaggregation of revenue

In the following table, revenue for the years ended December 31, 2020 and 2019 is disaggregated by type of service and timing of revenue recognition. Telecommunication service revenues are recognized over time and equipment sales at a point in time.

	2020	2019
<u>Regulated income:</u>		
Local network services	\$ 6,649,809	\$ 6,491,082
Network access services	10,757,151	11,636,935
Carrier billing and collections	335,155	253,174
Miscellaneous	505,804	649,457
Access revenue	7,000	44,000
	\$ 18,254,919	\$ 19,074,648
<u>Nonregulated income:</u>		
Customer premises equipment	\$ 1,008,873	\$ 760,340
Internet activities	3,865,406	3,583,483
Long distance services	357,922	449,477
Video services	3,503,422	3,212,642
Security/Surveillance/Bus Systems	524,030	685,760
	\$ 9,259,653	\$ 8,691,702

Contract cost liabilities

Contract cost liabilities include customer deposits. The balance in contract liabilities was \$260,694, \$211,235 and \$204,211 as of December 31, 2020, 2019, and 2018, respectively.

Note 14. Risks and Uncertainties

Local, U.S., and world governments have encouraged self-isolation to curtail the spread of the global pandemic, coronavirus disease (COVID-19), by mandating temporary work stoppage in many sectors and imposing limitations on travel and size and duration of group meetings. Most industries are experiencing disruption to business operations and the impact of reduced consumer spending. There is unprecedented uncertainty surrounding the duration of the pandemic, its potential economic ramifications, and any government actions to mitigate them. Accordingly, while management cannot quantify the financial and other impact to the Cooperative as of March 2, 2021, management believes that a material impact on the Cooperative's financial position and results of future operations is reasonably possible.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 15. Paycheck Protection Program Loan

In April 2020, the Cooperative applied for and was granted a forgivable loan of \$1,311,402 from the United States Small Business Administration (SBA) Paycheck Protection Program (PPP). Under the CARES Act, subject to limitations, as defined, the loan may be partially or fully forgiven, depending on specified actual payroll and other qualified costs for the covered period following receipt of the loan. Any amount not forgiven will be payable in 24 monthly installments of principal and interest at 1.00% and will be unsecured. The Cooperative accounted for the loan proceeds as debt in accordance with ASC 470. The Cooperative submitted its application for forgiveness to the SBA and was notified in December 2020 that the entire loan was forgiven. As such, the Cooperative, in compliance with guidance from RUS, has recognized the forgiveness of debt as other income for the qualified costs that were incurred during the covered period of the loan.

Note 16. Correction of Error

The Cooperative discovered it overstated accrued income taxes previously reported at December 31, 2019. The Cooperative has restated its 2019 previously issued consolidated financial statements to reflect the correction of an error. The effect of the correction increased income tax (benefit) expense from (\$894,618) to \$1,349,965 and decreased accrued income taxes from \$780,000 to \$130,988. The cumulative effect of the correction increased beginning patronage capital as of January 1, 2019 by \$2,893,595.

In addition, the Cooperative discovered it understated accumulated postretirement benefits previously reported as of December 31, 2019. The Cooperative has restated its 2019 previously issued consolidated financial statements to reflect the correction of an error. The effect of the correction increased accumulated postretirement benefits from \$2,779,504 to \$3,441,437 and increased accumulated postretirement expense included in other comprehensive income from \$3,591,156 to \$4,742,919.



Jones, Nale & Mattingly PLC

**INDEPENDENT AUDITOR'S REPORT ON
THE SUPPLEMENTARY INFORMATION**

To the Board of Directors
Mountain Rural Telephone Cooperative and Subsidiary
West Liberty, Kentucky

We have audited the consolidated financial statements of Mountain Rural Telephone Cooperative and Subsidiary as of December 31, 2020 and 2019, and our report thereon dated March 2, 2021, which expressed an unmodified opinion on those consolidated financial statements, appears on pages 1 and 2. Our audits were conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The supplementary information found on pages 23 and 24, is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The 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 information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

Jones, Nale & Mattingly PLC

Louisville, Kentucky
March 2, 2021

MOUNTAIN RURAL TELEPHONE COOPERATIVE AND SUBSIDIARY

CONSOLIDATING BALANCE SHEET

December 31, 2020

	Mountain Rural Telephone Cooperative	Mountain Telecommunications	Eliminations	Consolidated
ASSETS				
CURRENT ASSETS				
Cash and cash equivalents	\$ 21,712,108	\$ 15,569,363	\$ --	\$ 37,281,471
Accounts receivable, net	255,644	--	(18,167)	237,477
Other receivables	--	23	--	23
Materials and supplies, at average cost	1,153,997	--	--	1,153,997
Prepaid expenses	21,222	349,484	--	370,706
Total current assets	<u>23,142,971</u>	<u>15,918,870</u>	<u>(18,167)</u>	<u>39,043,674</u>
NON-CURRENT ASSETS				
Investment securities	12,805,931	--	--	12,805,931
Associated organizations	45,471,814	32,338,539	(45,471,814)	32,338,539
Pension plan prefunding	2,335,847	--	--	2,335,847
Nonregulated property	3,368,518	--	--	3,368,518
Total non-current assets	<u>63,982,110</u>	<u>32,338,539</u>	<u>(45,471,814)</u>	<u>50,848,835</u>
PROPERTY AND EQUIPMENT				
In service	135,666,963	3,000	--	135,669,963
Under construction	2,832,279	--	--	2,832,279
	<u>138,499,242</u>	<u>3,000</u>	<u>--</u>	<u>138,502,242</u>
Less accumulated depreciation	87,708,242	428	--	87,708,670
	<u>50,791,000</u>	<u>2,572</u>	<u>--</u>	<u>50,793,572</u>
	<u>\$ 137,916,081</u>	<u>\$ 48,259,981</u>	<u>\$ (45,489,981)</u>	<u>\$ 140,686,081</u>
LIABILITIES AND MEMBERS' EQUITIES				
CURRENT LIABILITIES				
Current portion of long-term debt	\$ 404,936	\$ --	\$ --	\$ 404,936
Accounts payable	616,732	18,167	(18,167)	616,732
Customer deposits	260,694	--	--	260,694
Accrued taxes	--	--	--	--
Accrued leave	2,204,488	--	--	2,204,488
Accrued expenses	120,661	--	--	120,661
Total current liabilities	<u>3,607,511</u>	<u>18,167</u>	<u>(18,167)</u>	<u>3,607,511</u>
NON-CURRENT LIABILITIES				
Long-term debt, less current portion	5,367,105	--	--	5,367,105
Accumulated postretirement benefits	4,109,527	--	--	4,109,527
Deferred tax liabilities	--	2,770,000	--	2,770,000
Total non-current liabilities	<u>9,476,632</u>	<u>2,770,000</u>	<u>--</u>	<u>12,246,632</u>
MEMBERS' EQUITIES				
Memberships and capital investments	137,116	4,780,000	(4,780,000)	137,116
Patronage capital and retained earnings	132,328,630	40,691,814	(40,691,814)	132,328,630
Donated capital	1,323,975	--	--	1,323,975
Accumulated other comprehensive (loss)	(8,957,783)	--	--	(8,957,783)
Total members' equities	<u>124,831,938</u>	<u>45,471,814</u>	<u>(45,471,814)</u>	<u>124,831,938</u>
	<u>\$ 137,916,081</u>	<u>\$ 48,259,981</u>	<u>\$ (45,489,981)</u>	<u>\$ 140,686,081</u>

MOUNTAIN RURAL TELEPHONE COOPERATIVE AND SUBSIDIARY
CONSOLIDATING STATEMENT OF INCOME AND COMPREHENSIVE INCOME
Year Ended December 31, 2020

	Mountain Rural Telephone Cooperative	Mountain Telecommunications	Eliminations	Consolidated
Operating revenues				
Local network service	\$ 6,649,809	\$ --	\$ --	\$ 6,649,809
Network access service	10,757,151	--	--	10,757,151
Carrier billing and collection	335,155	--	--	335,155
Miscellaneous	505,804	--	--	505,804
Access revenue	7,000	--	--	7,000
Total operating revenues	<u>18,254,919</u>	<u>--</u>	<u>--</u>	<u>18,254,919</u>
Operating expenses				
Plant specific operations	3,467,409	--	--	3,467,409
Plant non-specific	2,082,864	--	--	2,082,864
Depreciation	4,793,549	53	--	4,793,602
Customer operations	1,395,414	--	--	1,395,414
Corporate operations	1,937,594	16,503	--	1,954,097
Other deductions	111,535	--	--	111,535
Other taxes	882,133	141	--	882,274
Total operating expenses	<u>14,670,498</u>	<u>16,697</u>	<u>--</u>	<u>14,687,195</u>
Operating income (loss)	<u>3,584,421</u>	<u>(16,697)</u>	<u>--</u>	<u>3,567,724</u>
Other income (expenses)				
Interest income	329,733	126,189	--	455,922
Interest expense	(141,269)	--	--	(141,269)
Other income	1,422,227	--	--	1,422,227
Income in limited liability company	1,639,387	2,172,411	(1,639,387)	2,172,411
Total other income (expenses)	<u>3,250,078</u>	<u>2,298,600</u>	<u>(1,639,387)</u>	<u>3,909,291</u>
Income before income taxes	6,834,499	2,281,903	(1,639,387)	7,477,015
Income tax (expense)	<u>--</u>	<u>(642,516)</u>	<u>--</u>	<u>(642,516)</u>
Net income before nonregulated income	6,834,499	1,639,387	(1,639,387)	6,834,499
Nonregulated income	<u>2,461,485</u>	<u>--</u>	<u>--</u>	<u>2,461,485</u>
Net income	\$ 9,295,984	\$ 1,639,387	\$ (1,639,387)	\$ 9,295,984
Other comprehensive (loss)				
Accumulated postretirement expense	<u>(661,978)</u>	<u>--</u>	<u>--</u>	<u>(661,978)</u>
Total comprehensive income	<u>\$ 8,634,006</u>	<u>\$ 1,639,387</u>	<u>\$ (1,639,387)</u>	<u>\$ 8,634,006</u>



Jones, Nale & Mattingly PLC

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

To the Board of Directors
Mountain Rural Telephone Cooperative and Subsidiary
West Liberty, Kentucky

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 Mountain Rural Telephone and Cooperative (the Cooperative), as of and for the year ended December 31, 2020, and the related notes to the consolidated financial statements, and have issued our report thereon dated March 2, 2021.

Internal Control Over Financial Reporting

In planning and performing our audit of the consolidated financial statements, we considered the Cooperative'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 opinion on the consolidated financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Cooperative's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Cooperative's internal control over financial reporting.

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 the Cooperative's consolidated 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 Cooperative'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 Cooperative's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Jones, Nale & Mattingly P.C.

Louisville, Kentucky
March 2, 2021



Jones, Nale & Mattingly PLC

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

Board of Directors
Mountain Rural Telephone Cooperative and Subsidiary
West Liberty, Kentucky

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 Mountain Rural Telephone Cooperative and Subsidiary (the Cooperative), which comprise the balance sheet as of December 31, 2020, and the related statements of income and comprehensive income, changes in members' equities, and cash flows for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated March 2, 2021. In accordance with *Government Auditing Standards*, we have also issued our report dated March 2, 2021 on our consideration of the Cooperative'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 related to our audit have been furnished to management.

In connection with our audit, nothing came to our attention that caused us 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 and Grantees*, §1773.33, 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 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 our audit, we 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;
- 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 any Subsidiary as defined in Part 1773.33 (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 is listed below.

During 2004, the Cooperative formed a wholly-owned Subsidiary, Mountain Telecommunications, Inc., which provides telecommunications services outside of the Cooperative's service territory and is also 20% owner of East Kentucky Network, LLC, that provides cellular and other communication services in Eastern Kentucky. The initial investment was \$1,130,000. The investment in Mountain Telecommunications, Inc. is comprised of the following:

	<u>Investments</u>	<u>Profits</u>	<u>Total</u>
Beginning of year	\$ 4,780,000	\$ 39,050,397	\$ 43,830,397
Activity for 2020	--	1,641,417	1,641,417
End of year	<u>\$ 4,780,000</u>	<u>\$ 40,691,814</u>	<u>\$ 45,471,814</u>

The purpose of this report is solely to communicate, in connection with the audit of the consolidated financial statements, on compliance with aspects of contractual agreements and the regulatory requirements for telecommunication borrowers based on the requirements of 7 CFR Part 1773, Policy on Audits of Rural Utilities Service Borrowers and Grantees. Accordingly, this report is not suitable for any other purpose.

Jones, Nale & Mattingly P.C.

Louisville, Kentucky
March 2, 2021