

**SOUTH CENTRAL RURAL TELEPHONE
COOPERATIVE CORPORATION, INC.**

**Report on Audit of Financial Statements
and Supplemental Data**

**For the Years Ended
June 30, 2013 and 2012**

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CAMPBELL, MYERS AND RUTLEDGE, PLLC

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Independent Auditors' Report

Board of Directors
South Central Rural Telephone
Cooperative Corporation, Inc.

Glasgow, Kentucky 42141

Report on the Financial Statements

We have audited the accompanying financial statements of South Central Rural Telephone Cooperative Corporation, Inc., which comprise the balance sheets as of June 30, 2013 and 2012, and the related statements of operations, comprehensive income, changes in members' equity and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

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

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

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of South Central Rural Telephone Cooperative Corporation, Inc., as of June 30, 2013 and 2012, and the results of its operations and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated September 26, 2013, on our consideration of the South Central Rural Telephone Cooperative Corporation, Inc.¶ internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering South Central Rural Telephone Cooperative Corporation, Inc.¶ internal control over financial reporting and compliance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the South Central Rural Telephone Cooperative Corporation, Inc.¶ basic financial statements. The accompanying supplemental data on pages 18 and 19 is presented for purposes of additional analysis and are not a required part of the basic financial statements. This data the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedules of operating expenses in pages 18 and 19 are fairly stated in all material respects in relation to the basic financial statements as a whole.

Campbell, Myers & Rutledge, PLLC

Certified Public Accountants
September 26, 2013

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
BALANCE SHEETS
June 30, 2013 and 2012

	<u>2013</u>	<u>Restated 2012</u>
Current assets:		
Cash and cash equivalents	\$ 3,893,591	\$ 5,740,263
Temporary cash investments	1,700,000	1,700,000
Accounts and notes receivable, less allowance for doubtful accounts of \$25,486 in 2013 and \$21,330 in 2012	1,589,846	2,937,226
Materials and supplies at average cost	3,758,618	3,119,016
Accrued interest receivable	4,859	4,859
Prepaid expenses	<u>1,496,474</u>	<u>1,266,375</u>
Total current assets	<u>12,443,388</u>	<u>14,767,739</u>
Other assets:		
Marketable securities	38,128,085	30,185,026
Nonregulated investments	2,067,795	4,104,018
Investment in affiliated companies	74,404,753	70,082,534
Other deferred charges	<u>181,026</u>	<u>191,784</u>
Total other assets	<u>114,781,659</u>	<u>104,563,362</u>
Telephone plant, at cost (substantially all pledged as collateral on long- term debt to RUS):		
Telephone plant in service	171,350,387	165,037,295
Telephone plant under construction (estimating cost to complete \$0 in 2013 and \$0 in 2012)	<u>4,919,109</u>	<u>4,745,702</u>
Total	176,269,496	169,782,997
Less accumulated depreciation	<u>133,719,702</u>	<u>125,805,964</u>
Telephone plant, net	<u>42,549,794</u>	<u>43,977,033</u>
	<u>\$ 169,774,841</u>	<u>\$ 163,308,134</u>

	<u>2013</u>	Restated <u>2012</u>
Current liabilities:		
Current portion of long-term debt	\$ 2,988,642	\$ 2,868,156
Accounts payable	2,632,825	3,026,643
Accrued expenses	<u>2,919,488</u>	<u>2,727,109</u>
Total current liabilities	<u>8,540,955</u>	<u>8,621,908</u>
Long-term liabilities:		
Long-term obligation to RUS and RTB	278,252	406,575
Other long-term liabilities	<u>13,200,714</u>	<u>10,217,460</u>
Total long-term liabilities	<u>13,478,966</u>	<u>10,624,035</u>
Other Liabilities		
Deferred taxes	<u>15,233,447</u>	<u>14,260,312</u>
Total other liabilities	<u>15,233,447</u>	<u>14,260,312</u>
Commitments		
Members' equities:		
Patronage capital	61,346,791	67,265,361
Accumulated other comprehensive loss	(12,157,318)	(9,745,718)
Other equities	81,983,484	70,966,648
Other member capital	<u>1,348,516</u>	<u>1,315,588</u>
Total members' equities	<u>132,521,473</u>	<u>129,801,879</u>
	<u>\$ 169,774,841</u>	<u>\$ 163,308,134</u>

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

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
 STATEMENTS OF OPERATIONS
 For the Years Ended June 30, 2013 and 2012

	<u>2013</u>	<u>2012</u>
Operating revenues:		
Basic local network service	\$ 7,744,627	\$ 7,985,785
Network access services revenues	14,055,138	15,735,803
Carrier billing and collection	441,272	466,600
Miscellaneous	<u>1,149,695</u>	<u>1,074,385</u>
Total operating revenues	<u>23,390,732</u>	<u>25,262,573</u>
Operating expenses:		
Plant specific operations	4,568,821	4,508,131
Plant nonspecific operations	2,185,744	2,341,799
Depreciation and amortization	9,997,004	10,230,087
Customer operations	1,644,153	1,623,430
Corporate operations	2,703,853	3,077,046
Other operating taxes	<u>1,052,112</u>	<u>994,932</u>
Total operating expenses	<u>22,151,687</u>	<u>22,775,425</u>
Operating income	<u>1,239,045</u>	<u>2,487,148</u>
Nonoperating net income	20,973,355	19,019,760
Provision for income taxes	<u>(9,956,519)</u>	<u>(9,154,119)</u>
Income before interest charges	<u>12,255,881</u>	<u>12,352,789</u>
Interest on long-term debt to RUS, net of interest capitalized of \$220,370 in 2013 and \$126,841 in 2012	(186,607)	(306,319)
Nonregulated net income (loss)	<u>(4,687,026)</u>	<u>(2,462,708)</u>
Net income	<u>\$ 7,382,248</u>	<u>\$ 9,583,762</u>

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

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
STATEMENTS OF COMPREHENSIVE INCOME
For the Years Ended June 30, 2013 and 2012

	<u>2013</u>	Restated <u>2012</u>
Net income	\$ 7,382,248	\$ 9,583,762
Other comprehensive income (loss)		
Postretirement benefit other than pension:		
Unrecognized loss on assets	(2,411,600)	(3,269,173)
Transition obligation	<u>-</u>	<u>155,446</u>
Comprehensive income	<u>\$ 4,970,648</u>	<u>\$ 6,470,035</u>

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

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
STATEMENTS OF PATRONAGE CAPITAL AND OTHER EQUITIES
For the Years Ended June 30, 2013 and 2012

	Patronage Capital			Accumulated Other Comprehensive Income (Loss)	Other Equities
	Assignable	Assigned	Balance		
Balances, July 1, 2011, Restated	\$ 177,355	\$ 69,414,813	\$ 69,592,168	\$ (6,631,991)	\$ 61,101,007
Distribution of patronage capital	-	(2,024,929)	(2,024,929)	-	-
Patronage capital assigned for the year ended December 31, 2011	(73,805)	73,805	-	-	-
Retirement of patronage capital of estates of deceased members	-	(479,361)	(479,361)	-	-
Transfer of unclaimed patronage capital	459,362	-	459,362	-	-
Postretirement benefit other than pension					
Unrecognized loss on assets	-	-	-	(3,269,173)	-
Transition obligation	-	-	-	155,446	-
Net income for the year ended June 30, 2012:					
Operating margins	(281,879)	-	(281,879)	-	-
Nonoperating margins	-	-	-	-	9,865,641
Balances, June 30, 2012, Restated	281,033	66,984,328	67,265,361	(9,745,718)	70,966,648
Distribution of patronage capital	-	(2,039,255)	(2,039,255)	-	-
Patronage capital assigned for the year ended December 31, 2012	(882,477)	882,477	-	-	-
Retirement of patronage capital of estates of deceased members	-	(505,994)	(505,994)	-	-
Transfer of unclaimed patronage capital	261,267	-	261,267	-	-
Postretirement benefit other than pension					
Unrecognized loss on assets	-	-	-	(2,411,600)	-
Transition obligation	-	-	-	-	-
Net income for the year ended June 30, 2013:					
Operating margins	(3,634,588)	-	(3,634,588)	-	-
Nonoperating margins	-	-	-	-	11,016,836
Balances, June 30, 2013	<u>\$ (3,974,765)</u>	<u>\$ 65,321,556</u>	<u>\$ 61,346,791</u>	<u>\$ (12,157,318)</u>	<u>\$ 81,983,484</u>

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

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
STATEMENTS OF CASH FLOWS
For the Years Ended June 30, 2013 and 2012

	<u>2013</u>	<u>Restated 2012</u>
Cash flows from operating activities:		
Net income	\$ 7,382,248	\$ 9,583,762
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	9,997,004	10,230,087
Deferred taxes on income	973,135	4,504,119
Changes in operating assets and liabilities:		
Decrease (increase) in temporary cash investments	-	-
Decrease (increase) in accounts and notes receivable	1,347,380	(1,515,827)
Decrease (increase) in inventory	(639,602)	297,103
Decrease (increase) in prepaid expenses	(230,099)	(117,801)
Increase (decrease) in accounts payable	(393,818)	(104,941)
Increase (decrease) in accrued expenses	<u>192,379</u>	<u>18,796</u>
Net cash provided by operating activities	<u>18,628,627</u>	<u>22,895,298</u>
Cash flows from investing activities:		
Purchases of property, plant and equipment	(6,471,634)	(7,587,732)
Plant removal costs	(120,861)	(64,925)
Salvage recovered from retirement of plant	154,990	205,756
Decrease (increase) in nonregulated investment	2,036,223	1,038,913
Decrease (increase) in other deferred charges	10,758	(25,593)
(Increase) in investment in affiliated companies	(4,322,219)	(7,522,275)
Purchases of Marketable Securities	(19,437,978)	(12,118,070)
Redemptions of Marketable Securities	<u>11,494,919</u>	<u>5,918,129</u>
Net cash used in investing activities	<u>(16,655,802)</u>	<u>(20,155,797)</u>

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

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
 STATEMENTS OF CASH FLOWS, CONCLUDED
 For the Years Ended June 30, 2013 and 2012

	<u>2013</u>	<u>Restated 2012</u>
Cash flows from financing activities:		
Distributions of patronage capital	\$ (2,039,255)	\$ (2,024,929)
Retirements of patronage capital	(505,994)	(479,361)
Principal payments to Rural Utilities Service	-	(216,791)
Principal payments to Federal Financing Bank	(2,140,097)	(2,746,120)
Increase (decrease) in long-term liabilities	571,654	89,369
Increase (decrease) in other member capital	32,928	(165,482)
Transfers of unclaimed patronage capital	<u>261,267</u>	<u>459,362</u>
Net cash provided (used) in financing activities	<u>(3,819,497)</u>	<u>(5,083,952)</u>
Net increase (decrease) in cash and cash equivalents	(1,846,672)	(2,344,451)
Cash and cash equivalents at beginning of year	<u>5,740,263</u>	<u>8,084,714</u>
Cash and cash equivalents at end of year	<u>\$ 3,893,591</u>	<u>\$ 5,740,263</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest (\$220,370 capitalized in 2013 and 126,842 in 2012)	<u>\$ 304,977</u>	<u>\$ 405,723</u>
Income taxes	<u>\$ 8,983,384</u>	<u>\$ 4,650,000</u>

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

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2013 and 2012

1. Summary of Significant Accounting Policies:

General:

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

Nature of Business:

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

Estimates:

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

Telephone Plant:

The telephone plant in service and under construction at June 30, 2013 and 2012 is stated substantially at original cost, which includes material, labor, transportation and such indirect items as engineering, supervision, employee fringe benefits and interest on funds used during construction. As property units are retired in the ordinary course of business, the cost of the property plus removal cost, less salvage, is charged to accumulated depreciation. Listed below are the major classes of the telephone plant as of June 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>	<u>Depreciation Rate</u>
Organization	\$ 20,039	\$ 20,039	-
Land	514,751	514,751	-
Buildings	7,577,731	7,538,363	2.70%
Central Office Equipment	50,003,365	49,045,022	7.5-11.9%
Station Equipment	997,697	997,697	-
Cable and Wire Facilities	102,738,620	97,375,060	2.2-9.4%
Furniture and Office Equipment	712,918	778,122	7.50%
General Purpose Computers	3,752,049	3,700,287	15.80%
Vehicles	4,897,697	4,932,434	10.1-12.1%
Garage and Work Equipment	135,520	135,520	7.50%
	<u>\$ 171,350,387</u>	<u>\$ 165,037,295</u>	

Depreciation:

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

Depreciation for the years ended June 30, 2013 and 2012 was \$9,997,004 and \$10,230,087, respectively.

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2013 and 2012

1. Summary of Significant Accounting Policies, Continued:

Deregulated Customer Premises Equipment:

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

Nonregulated Investments:

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

Following is a summary of net income (loss) from deregulated operations for the years ending June 30, 2013 and 2012:

	<u>2013</u>	<u>2012</u>
Income from operations	\$ 14,682,020	\$ 14,522,568
Expenses	<u>(19,369,046)</u>	<u>(16,985,276)</u>
Net income (loss)	<u>\$ (4,687,026)</u>	<u>\$ (2,462,708)</u>

Cash and Cash Equivalents:

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

Accounts and Notes Receivable:

Included in accounts and notes receivable at June 30, 2013 and 2012, is unbilled revenue of \$36,124 and \$79,115, respectively. The Company estimates uncollectable accounts as a percentage of monthly revenues and compares this to invoices dated over 90 days when they are considered uncollectible. The board of directors write off receivables as a charge to the allowance for credit losses, in their estimation, it is probable that the receivable is worthless.

Other Member Capital:

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

Inventories:

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

Subsequent Events:

Management has evaluated subsequent events through September 26, 2013, the date which the financial statements were available to be issued.

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2013 and 2012

1. Summary of Significant Accounting Policies, Concluded:

Reclassifications:

Certain reclassifications have been made to the 2012 financial statement presentation to correspond to the current year's format. Total equity and net income are unchanged due to these reclassifications.

Related Party Transactions:

The Company was indebted to 100% owned subsidiary (South Central Telcom, LLC) in the amount of \$1,031,792 and \$976,473 for the years ended June 30, 2013 and 2012 respectively.

South Central Telcom, LLC pays South Central Rural Telephone Cooperative for switch port costs and billing and collection services on a monthly basis.

Investment in Affiliated Companies:

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

	<u>Percentage Owned</u>	<u>2013</u>	<u>2012</u>
RSA #3 Partnership	25%	\$ 18,045,416	\$ 17,368,627
RSA #4 Partnership	50%	29,896,129	27,713,175
Cumberland Cellular Partnership	12.5%	6,979,500	6,712,007
Bluegrass Network, LLC	20%	3,649,613	2,995,229
Bluegrass Telcom, LLC	20%	325,420	339,968
South Central Telcom, LLC	100%	15,508,675	14,953,528
		<u>\$ 74,404,753</u>	<u>\$ 70,082,534</u>

2. Commitments:

In June, 1994, the Cooperative executed notes to RUS and the Rural Telephone Bank in the amount of \$13,435,000 and \$13,559,700, respectively. These funds are being used to finance construction of additional telephone lines and facilities and the operation of the telephone system. As of June 30, 2013, \$22,384,918 of these funds have been advanced. At June 30, 2013, construction contracts for approximately \$27,000,000 have been awarded.

3. Long-Term Debt:

Long-term debt is represented by mortgage notes payable to the United States of America. Principal and interest payments are due in quarterly installments. It is estimated that quarterly installments of \$750,000 are payable within the next twelve months. The notes are scheduled to be repaid during the year 2015. At June 30, 2013, the Cooperative has advance payments in amount of \$5,170,380 that may be applied to the installments after the application of \$2,456,730 during the current year.

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2013 and 2012

3. Long-Term Debt, Concluded:

	<u>2013</u>	<u>2012</u>
Due to United States of America		
4.1710% First Mortgage Notes - FFB	\$ 8,437,274	\$ 10,577,372
Advance Payments	<u>5,170,380</u>	<u>7,302,641</u>
	3,266,894	3,274,731
Less current maturities	<u>(2,988,642)</u>	<u>(2,868,156)</u>
Total	<u>\$ 278,252</u>	<u>\$ 406,575</u>

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

2014	\$ 2,988,642
2015	<u>278,252</u>
Total	<u>\$ 3,266,894</u>

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

4. Cash and Cash Equivalents:

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

	2013		2012	
	Carrying Amount	Bank Balance	Carrying Amount	Bank Balance
Insured (FDIC)	\$ 3,893,591	\$ 4,178,619	\$ 5,704,140	\$ 6,262,709
Uninsured:				
Uncollateralized	<u>-</u>	<u>82,506</u>	<u>36,123</u>	<u>32,698</u>
Total deposits	<u>\$ 3,893,591</u>	<u>\$ 4,261,125</u>	<u>\$ 5,740,263</u>	<u>\$ 6,295,407</u>

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2013 and 2012

5. Pension Plan:

The Cooperative has a defined benefit pension plan covering substantially all of its employees. In October, 1988, the Cooperative approved the retroactive purchase of all prior service benefits as of December 31, 1988, at a cost of \$487,804. Contributions to the Plan for the years ended June 30, 2013 and 2012 were \$989,677 and \$773,130, respectively. The Plan has been approved by the Internal Revenue Service. As the Cooperative is only one of several employers participating in the Plan, it is not practicable to determine if the vested benefits of the Cooperative's employees exceed the Cooperative's portion of the Plan assets.

The following table presents certain information regarding the Plan's status as a whole, derived from actuarial valuations performed as of the dates indicated:

	<u>Pension Benefits</u>	
	<u>January 1, 2013</u>	<u>January 1, 2012</u>
Fair value of plan assets	\$ 1,368,763,503	\$ 1,380,786,158
Present value of accumulated benefits	<u>(1,386,628,324)</u>	<u>(1,267,739,443)</u>
Overfunded/(Unfunded)	<u>\$ (17,864,821)</u>	<u>\$ 113,046,715</u>

	<u>Pension Benefits</u>	
	<u>January 1, 2013</u>	<u>January 1, 2012</u>
Weighted . average assumptions as of January 1:		
Valuation interest rate	7.50%	7.50%
Expected return on plan assets	7.50%	7.50%
Rate of compensation increase	age related	age related

6. Income Taxes:

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

The provision for income taxes for 2013 and 2012 consists of the following:

Provision for Income Taxes:	<u>2013</u>	<u>2012</u>
Current tax expense	\$ 8,983,384	\$ 4,650,000
Deferred tax (benefit)	<u>973,135</u>	<u>4,504,119</u>
Total	<u>\$ 9,956,519</u>	<u>\$ 9,154,119</u>

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
 NOTES TO FINANCIAL STATEMENTS
 June 30, 2013 and 2012

6. Income Taxes, Concluded:

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

	<u>2013</u>	<u>2012</u>
Differences in depreciation methods	<u>\$ 15,233,447</u>	<u>\$ 14,260,312</u>

The Company follows the recognition requirements for uncertain income tax positions as required by generally accepted accounting principles. The Company has no tax position at June 30, 2013 for which the ultimate deductibility is highly certain but for which there is uncertainty about the timing of such deductibility. The Company's policy is to classify income tax related interest and penalties in interest expense and other expenses, respectively. No such interest or penalties were recognized during the periods presented.

The Company files income tax returns in the U.S. federal jurisdiction, and various state and local jurisdictions. The Company is no longer subject to U.S. federal, state and local income tax examinations by tax authorities for years before 2010.

7. Marketable Securities:

The maturities of held to maturity investments and their approximate market values at June 30, 2013 and 2012, were as follows:

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

	Amortized Cost	Net Unrealized Gains (Losses)	Market Value
June 30, 2013	\$ 39,828,085	\$ (1,844,966)	\$ 37,983,119
June 30, 2012	\$ 31,885,026	\$ 165,893	\$ 32,050,919
June 30, 2011	\$ 25,685,084	\$ (181,690)	\$ 25,503,394
		Amortized Cost	Market Value
Due in one year or less (included in Temporary Cash Investments)		\$ 1,700,000	\$ 1,700,000
Due after one year		<u>38,128,085</u>	<u>36,283,119</u>
Balances, June 30, 2013		<u>\$ 39,828,085</u>	<u>\$ 37,983,119</u>
Due in one year or less (included in Temporary Cash Investments)		\$ 1,700,000	\$ 1,700,000
Due after one year		<u>30,185,026</u>	<u>30,350,919</u>
Balances, June 30, 2012		<u>\$ 31,885,026</u>	<u>\$ 32,050,919</u>

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2013 and 2012

8. Postretirement Benefits:

The Corporation sponsors a defined benefit plan that provides medical and life insurance coverage to retirees and their dependents. Participating retirees and dependents contribute 0% of the projected cost of coverage. The plan is partially funded.

The following sets forth the accumulated post-retirement benefit obligation, the change in plan assets, and the component of accrued post-retirement benefit cost and net periodic benefit cost as of June 30, 2013 and 2012.

	<u>2013</u>	<u>2012</u>
Accumulated post-retirement benefit obligation, beginning	\$ 23,715,063	\$ 19,827,883
Service cost	1,004,664	792,522
Interest cost	1,258,028	1,165,643
Plan Participants contributions	989,676	773,130
Actuarial loss	2,237,779	1,964,502
Benefits paid	<u>(815,061)</u>	<u>(790,617)</u>
Accumulated post retirement benefit obligation, ending	<u>\$ 28,390,149</u>	<u>\$ 23,715,063</u>
Fair value of plan assets - beginning of year	\$ 12,683,239	\$ 12,098,933
Employer contributions	924,925	708,440
Plan Participants contributions	64,751	64,690
Unrealized gains on assets	1,458,112	601,793
Benefits paid	<u>(815,061)</u>	<u>(790,617)</u>
Fair value of plan assets - end of year	<u>14,315,966</u>	<u>12,683,239</u>
Unfunded status	\$ 14,074,183	\$ 11,031,824
Unrecognized net actuarial loss	<u>12,157,319</u>	<u>9,749,810</u>
Net amount recognized	<u>\$ 26,231,502</u>	<u>\$ 20,781,634</u>
Unfunded status	\$ 14,074,183	\$ 11,031,824
Current liabilities	<u>877,560</u>	<u>814,364</u>
Noncurrent liabilities	<u>\$ 13,196,623</u>	<u>\$ 10,217,460</u>
Service cost	\$ 1,004,664	\$ 792,522
Interest cost	1,258,028	1,165,643
Amortization of net actuarial gain	526,264	566,116
Expected return on assets	<u>(1,039,357)</u>	<u>(920,823)</u>
Net periodic benefit cost	<u>\$ 1,749,599</u>	<u>\$ 1,603,458</u>
Net amount recognized (included in other comprehensive income)	<u>\$ (2,411,600)</u>	<u>\$ (3,113,727)</u>
Amounts in other comprehensive income expected to be realized in the subsequent year - actuarial gain	<u>\$ 526,264</u>	<u>\$ 566,116</u>

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
NOTES TO FINANCIAL STATEMENTS
June 30, 2013 and 2012

8. Postretirement Benefits:

The Discount rate used in determining the accumulated postretirement benefit obligation was 4.5% and 5% for the years ending June 30, 2013 and 2012, respectively.

Expected benefit payments from the plan for year ending June 30, 2014 total \$877,560.

For measurement purposes, an 8% annual rate of increase in the per capita cost of covered health care benefits was used for the year ended June 30, 2013. The anticipated future rates are as follows:

2014	7.00%
2015	6.00%
2016	5.50%
2017	5.00%
2018	5.00%

An additional 1% increase in the trend utilized for measurement purposes in 2013 would have resulted in an increase in the accumulated postretirement benefit obligation of approximately 5.5 million.

9. Restatement of Previously Issued Financial Statements:

The Company has restated its previously issued financial statements for June 30, 2012, primarily to reflect the correction of errors related to its post retirement benefit obligation.

GAAP requires that companies recognize the funded status of the single employer benefit plan in its financial statements. Also, as a component of other comprehensive income, the company must also recognize the gains and losses that arise during the period associated with the plan.

The effect on previously issued financial statements is as follows:

	<u>June 30, 2012</u>
Members Equities:	
Patronage Capital	
As Previously Reported	\$ 65,194,280
As Restated	\$ 67,265,361
Accumulated other comprehensive loss	
As Previously Reported	\$ -
As Restated	\$ (9,745,718)
Other Long-Term Liabilities:	
As Previously Reported	\$ 2,835,595
As Restated	\$ 10,217,460
Other Comprehensive Loss	
As Previously Reported	\$ -
As Restated	\$ (3,113,727)

SUPPLEMENTAL DATA

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
 STATISTICAL AND ANALYTICAL INFORMATION
 June 30, 2013, 2012

	2013	2012	2011
<u>Telephone Plant in Service - June 30:</u>	\$ 171,350,387	\$ 165,037,295	\$ 159,052,610
Investment per subscriber - June 30	7,021	6,622	6,271
Investment per dollar of operating revenue	6.62	6.38	6.15
<u>Depreciation Reserve - June 30:</u>	133,719,702	125,805,964	116,510,825
Percent of plant in service	78.04%	76.23%	73.25%
Annual depreciation	9,997,004	10,230,087	10,435,074
Percent of annual depreciation to plant in service	5.83%	6.20%	6.56%
<u>Average Annual Revenue Per Subscriber:</u>			
Local service	317	320	319
Toll service and access charges	594	650	616
Total operating revenue	958	1,014	976
<u>Number of Stations - June 30:</u>			
Residence:			
Main stations	21,189	21,654	21,998
Business:			
Main stations (access lines)	3,215	3,269	3,365
Total main stations	24,404	24,923	25,363

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

SOUTH CENTRAL RURAL TELEPHONE COOPERATIVE CORPORATION, INC.
 STATISTICAL AND ANALYTICAL INFORMATION, CONCLUDED
 June 30, 2013 and 2012

	2013		Restated 2012		Restated 2011	
	Amount	Percent	Amount	Percent	Amount	Percent
Local network service	\$ 7,744,627	33.11%	\$ 7,985,785	31.61%	\$ 8,094,575	32.69%
Network access and long- distance network service	14,055,138	60.09%	15,735,803	62.29%	15,151,502	61.20%
Miscellaneous	<u>1,590,967</u>	<u>6.80%</u>	<u>1,540,985</u>	<u>6.10%</u>	<u>1,512,654</u>	<u>6.11%</u>
Total operating revenue	<u>23,390,732</u>	<u>100.00%</u>	<u>25,262,573</u>	<u>100.00%</u>	<u>24,758,731</u>	<u>100.00%</u>
Cost of telephone service, net of other income and expenses	<u>16,008,484</u>	<u>68.44%</u>	<u>15,678,811</u>	<u>62.06%</u>	<u>16,980,422</u>	<u>68.58%</u>
Net income	<u>\$ 7,382,248</u>	<u>31.56%</u>	<u>\$ 9,583,762</u>	<u>37.94%</u>	<u>\$ 7,778,309</u>	<u>31.42%</u>
 <u>Source of Funds Invested in</u>						
<u>Total Assets:</u>						
Members' equities	\$ 132,521,473	78.06%	\$ 129,801,879	79.48%	\$ 125,542,254	81.54%
Long-term liabilities	28,712,413	16.91%	24,884,347	15.24%	19,620,314	12.74%
Other liabilities	<u>8,540,955</u>	<u>5.03%</u>	<u>8,621,908</u>	<u>5.28%</u>	<u>8,802,809</u>	<u>5.72%</u>
Total assets	<u>\$ 169,774,841</u>	<u>100.00%</u>	<u>\$ 163,308,134</u>	<u>100.00%</u>	<u>\$ 153,965,377</u>	<u>100.00%</u>



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Independent Auditor's Report on Internal Control over Financial Reporting
and on Compliance and Other Matters Based on an Audit
of Financial Statements Performed in
Accordance With *Government Auditing Standards*

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

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the of South Central Rural Telephone Cooperative Corporation, Inc. as of and for the years ended June 30, 2013 and 2012, and the related statements of operations, comprehensive income, changes in member's equity and cash flows for the years then ended, and the related notes to the financial statements, and have issued our report thereon dated September 26, 2013.

Internal Control over Financial Reporting

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

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

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

Compliance and Other Matters

As part of obtaining reasonable assurance about whether South Central Rural Telephone Cooperative Corporation, Inc.'s financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts.

However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

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

Campbell, Myers & Rutledge, PLLC

Certified Public Accountants
September 26, 2013

