

## MEMORANDUM

August 14, 2015

TO: Board of Directors  
FROM: Foster Hildreth, General Manager  
RE: Rock Island Communications; Second Quarter Financial Review

The Q2 (YTD) of full operations of Rock Island Communications was a progressive move towards our full operating model and goals. We are nearing completion for our integration efforts. The Q2 financials are attached.

Our primary focus in Q2 was the construction efforts of Middle Mile infrastructure in Spring Point, The Cape, Mineral Point, Eagle Lake and Alder Cottages. In addition, we continued to fill our pipeline of fiber-hoods and new connections along with supporting all existing revenue streams.

### **Operational Milestones achieved in Q2 2015**

- Managed simultaneous construction efforts on multiple islands completing the development of Eagle Lake, Alder Cottages and numerous individual connections
- County wide engagement of all emergency services to co-develop a data network for county wide use.
- Completed contract and tech specs on SIM cards for LTE Network.
- Completed comprehensive Radio Frequency study for optimal LTE deployment.
- Began development on a county wide fiber/LTE cost estimation model to predicate individual and collective costs of deployment.
- Hired key staff in sales and operations.
- Achieved 2 additional HOA fiber-hood build commitments
  - Alder Forest (Orcas)
  - Whiskey Hill (Lopez)
- Delivered 48 new fiber to the home services.
- Started delivering VoIP services.

### **Operational Challenges in Q2 2015**

- LTE build out is going slower than planned, due to vendor selection and system testing.
- VoIP has been a greater challenge and steeper learning curve than anticipated. The transfer process from CenturyLink is frustrating and overly complex.
- Inquiry and Prospect Volume – Effective county wide communication continues to be a challenge, especially in real-time to various groups and individuals. We expect this to improve significantly throughout the balance of 2015 as we implement our operational platforms and tracking systems.

## Financial Highlights for Q2 2015

The budget to actual performance for Island Network overall remains in-line with expectations for the first half of the year.

Revenues came in just above budget for the half at \$811,766 with a variance of \$23,158 from budget. Operating Expenses were lower than budget at \$978,088, \$186,999 under budget.

An important risk-mitigating factor within the business plan is to correlate a significant portion of the tranche investment structure to the take rate as well as the addition of Rock Island legacy revenue stream. We are now accelerating our LTE construction investment in order to deliver approximately 600 fixed wireless subscribers before year end.

Table 1

|                     | Budget Period End | Actual Period End | Variance    |
|---------------------|-------------------|-------------------|-------------|
| <b>Op Revenue</b>   | \$788,609         | \$811,766         | \$23,158    |
| <b>COGS</b>         | \$338,511         | \$336,409         | (\$2,102)   |
| <b>Gross Profit</b> | \$450,098         | \$475,357         | \$25,259    |
| <b>Op Expenses</b>  | \$1,165,087       | \$978,088         | (\$186,999) |
| <b>Net Margin</b>   | (\$738,121)       | \$(522,392)       | \$215,729   |

## Borrowings from OPALCO (Nov 14 to Period End)

Borrowings for the year adjusted for the acquisition of Rock Island Technology Solutions is \$3.4M, up from \$2.9M. Through the first eight months (Nov, Dec 14 & Q1 & Q2 15) our borrowings from OPALCO totals \$2.8M for startup costs and connection incentives. The remaining amount is in line with our running operational costs for the balance of 2015.

## Staffing

In line with budgeted expectations after the acquisition staffing levels at period end where 17 FTE's compared to a budgeted 19 FTE's.

Positions filled by period end;

1. EVP
2. VP Operations
3. VP Technology
4. VP Engineering
5. VP Sales and Marketing
6. Network Operations
7. Customer Support
8. Retail Sales
9. System Admin
10. GIS Tech
11. Field Tech +5
12. Operations Support +3

## Subscriber Highlights for Q1 2015

Our goals planned for a gradual ramp up in subscribers during the initial months of 2015 continues particularly those receiving Fiber to the home. Q2 of 2015 was focused on gearing up and beginning our first group of large fiber-hoods. Initial construction efforts have been a mix of great to moderate. Two major projects (Spring Point & Mineral Point) have had two very different middle mile experiences. The Spring Point middle mile project went exceedingly well, on time and on budget. The Mineral Point middle mile, while on budget, has taken far too long with a significant impact on the homeowners.

Total new fiber subscribers for 2015 were budgeted to be 400. As of end of Q2 we have added 68 new subscribers. We currently have fiber under construction to 278 properties with an expected 255 new connections from these. We are expecting 185 new connections to occur in Q3. The table below lays out our overall progress by subscriber type and compares budget to actual.

### ROCK ISLAND COMMUNICATIONS

#### Total Subscribers - Budget To Actual

| BUDGET                     | 2014            | 2015 Budget |             |             |             | Comments                |
|----------------------------|-----------------|-------------|-------------|-------------|-------------|-------------------------|
|                            | Actual Year-end | 1st Quarter | 2nd Quarter | 3rd Quarter | 4th Quarter |                         |
| Subscribers                |                 |             |             |             |             |                         |
| DSL                        |                 | 1,444       | 1,444       | 1,444       | 1,444       |                         |
| Canopy                     |                 | 174         | 174         | 174         | 174         |                         |
| Fiber                      |                 | 138         | 178         | 328         | 500         |                         |
| LTE                        |                 | 100         | 250         | 400         | 608         |                         |
| Total                      |                 | 1,856       | 2,046       | 2,346       | 2,726       |                         |
| ACTUAL                     | 2014            | 2015 Actual |             |             |             | Comments                |
| Subscribers                | Actual Year-end | 1st Quarter | 2nd Quarter | 3rd Quarter | 4th Quarter |                         |
| DSL                        | -               | 1,444       | 1,470       |             |             | Delay in LTE Deployment |
| Canopy                     | -               | 174         | 174         |             |             |                         |
| Fiber                      | 108             | 128         | 176         |             |             |                         |
| LTE                        | -               | -           | -           |             |             |                         |
| Total                      | 108             | 1,746       | 1,820       | -           | -           |                         |
| Variance (Actual - Budget) | -               | (110)       | (226)       | -           | -           |                         |

\*We project that budgeted LTE subscriptions will be connected by year end.

# ISLAND NETWORK

## STATEMENT OF OPERATIONS BUDGET

|                                                  | A.                      | B.                                     | C.                                              |
|--------------------------------------------------|-------------------------|----------------------------------------|-------------------------------------------------|
|                                                  | Rock Island Budget 2015 | Island Network<br>Proposed Budget 2015 | Island Network Annual<br>Budget 2015<br>(A + B) |
| 1 <b>I OPERATING REVENUES</b>                    |                         |                                        |                                                 |
| 2     Sales                                      | \$ 1,081,518            | \$ 1,171,650                           | \$ 2,253,168                                    |
| 3 <b>TOTAL OPERATING REVENUES</b>                | <b>1,081,518</b>        | <b>1,171,650</b>                       | <b>2,253,168</b>                                |
| 4                                                |                         |                                        |                                                 |
| 5 <b>II COST OF GOODS SOLD</b>                   | 674,374                 | 292,800                                | 967,174                                         |
| 6 <b>TOTAL COST OF GOODS SOLD</b>                | <b>674,374</b>          | <b>292,800</b>                         | <b>967,174</b>                                  |
| 7 <b>Gross Profit</b>                            | <b>407,144</b>          | <b>878,850</b>                         | <b>1,285,994</b>                                |
| 8 <b>III OPERATING EXPENSES</b>                  |                         |                                        |                                                 |
| 9     Advertising                                | -                       | 75,000                                 | 75,000                                          |
| 10    Depreciation Expense                       | 37,890                  | 187,166                                | 225,056                                         |
| 11    Insurance                                  | -                       | 100,000                                | 100,000                                         |
| 12    Interest Expense                           | 36,000                  | 174,000                                | 210,000                                         |
| 13    Office Expenses                            | -                       | -                                      | -                                               |
| 14    Payroll Expenses                           | 395,638                 | 929,500                                | 1,325,138                                       |
| 15    Professional Fees                          | -                       | 200,000                                | 200,000                                         |
| 16    Rent                                       | -                       | 120,000                                | 120,000                                         |
| 17    Utilities                                  | (42,000)                | 172,000                                | 130,000                                         |
| 18    Other                                      | (94,695)                | 94,695                                 | -                                               |
| 19    Travel & Ent                               | -                       | 20,000                                 | 20,000                                          |
| 20 <b>TOTAL OPERATING EXPENSES</b>               | <b>332,833</b>          | <b>2,072,361</b>                       | <b>2,405,193</b>                                |
| 21 <b>TOTAL NET OPERATING MARGINS</b>            | <b>\$ 74,311</b>        | <b>\$ (1,193,511)</b>                  | <b>\$ (1,119,199)</b>                           |
| 22 <b>IV OTHER INCOME (EXPENSE)</b>              |                         |                                        |                                                 |
| 23     Interest Income                           | -                       | -                                      | -                                               |
| 24     Other Income (Expense)                    | -                       | -                                      | -                                               |
| 25     Taxes: Property Taxes                     | 25,000                  | (25,000)                               | -                                               |
| 26     Taxes: State & Local Use Tax              | (16,174)                | (30,089)                               | (46,263)                                        |
| 27 <b>TOTAL OTHER INCOME</b>                     | <b>8,826</b>            | <b>(55,089)</b>                        | <b>(46,263)</b>                                 |
| 28 Federal Income Tax Expense                    | -                       | -                                      | -                                               |
| 29 <b>GRAND TOTAL NET MARGIN DETAIL BREAKOUT</b> | <b>83,137</b>           | <b>(1,248,599)</b>                     | <b>(1,165,462)</b>                              |
| <b>TOTAL EXPENSES</b>                            | <b>\$ 998,381</b>       | <b>\$ 2,420,249</b>                    | <b>\$ 3,418,630</b>                             |

ISLAND NETWORK  
STATEMENT OF OPERATIONS BUDGET TO ACTUAL  
DETAILED BREAKOUT OF NOTABLE DRIVERS

|                                                              | A.<br>Island Network Budget<br>Annual<br>2015 | B.<br>Island Network Budget<br>Period End<br>6/30/2015 | C.<br>Island Network Actual<br>Period End<br>6/30/2015 | D.<br>Variance<br>(C-B) | I.<br>Comments: Period End Budget To Actual                                                                                                                       |
|--------------------------------------------------------------|-----------------------------------------------|--------------------------------------------------------|--------------------------------------------------------|-------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1 I OPERATING REVENUES                                       | \$ 2,253,168                                  | \$ 788,609                                             | \$ 811,766                                             | \$ 23,158               |                                                                                                                                                                   |
| 2 Operating Revenue - Line 6 Detail Breakout                 |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 3                                                            |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 4                                                            |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 5 Other Operating Revenue                                    |                                               | 788,609                                                | 811,766                                                | 23,158                  |                                                                                                                                                                   |
| 6 TOTAL OPERATING REVENUES                                   | 2,253,168                                     | 788,609                                                | 811,766                                                | 23,158                  | Due to delay deployment of LTE expected shortfall in Revenue compared to full year budget (-\$350k). Connections still expected to be in line with year end goals |
| 7                                                            |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 8 II COST OF GOODS SOLD                                      | 967,174                                       | 338,511                                                | 336,409                                                | (2,102)                 |                                                                                                                                                                   |
| 9 COGS - Line 15 Detail Breakout                             |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 10                                                           |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 11                                                           |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 12                                                           |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 13                                                           |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 14 Other Cost of Goods Sold                                  |                                               | 338,511                                                | 336,409                                                | (2,102)                 |                                                                                                                                                                   |
| 15 TOTAL COST OF GOODS SOLD                                  | 967,174                                       | 338,511                                                | 336,409                                                | (2,102)                 |                                                                                                                                                                   |
| 16 Gross Profit                                              | 1,285,994                                     | 450,098                                                | 475,357                                                | 25,259                  |                                                                                                                                                                   |
| 17                                                           |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 18 III OPERATING EXPENSES                                    | 2,405,193                                     | 1,165,087                                              | 978,088                                                | (186,999)               |                                                                                                                                                                   |
| 19 Operating Expenses - Line 25 Detail Breakout              |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 20 Payroll Expenses                                          |                                               | 662,569                                                | 555,651                                                | (106,918)               |                                                                                                                                                                   |
| 21 Professional Fees                                         |                                               | 100,000                                                | 204,499                                                | 104,499                 | Offset between outside contracting versus FTE's                                                                                                                   |
| 22 Rent                                                      |                                               | 60,000                                                 | 48,759                                                 | (11,241)                |                                                                                                                                                                   |
| 23 Utilities                                                 |                                               | 65,000                                                 | 3,658                                                  | (61,342)                |                                                                                                                                                                   |
| 24 Other                                                     |                                               | 277,519                                                | 165,522                                                | (111,997)               | Marketing, Depreciation, Insurance, Rent etc                                                                                                                      |
| 25 TOTAL OPERATING EXPENSES                                  | 2,405,193                                     | 1,165,087                                              | 978,088                                                | (186,999)               |                                                                                                                                                                   |
| 26 TOTAL NET OPERATING MARGINS                               | \$ (1,119,199)                                | \$ (714,990)                                           | \$ (502,731)                                           | \$ 212,259              |                                                                                                                                                                   |
| 27                                                           |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 28 IV NON-OPERATING MARGINS (EXPENSE)                        | (46,263)                                      | (23,131)                                               | (19,661)                                               | 3,470                   |                                                                                                                                                                   |
| 29 Non-operating Margins (Expense) - Line 35 Detail Breakout |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| 30 Interest Income                                           |                                               | -                                                      | 157                                                    | 157                     |                                                                                                                                                                   |
| 31 Other Income (Expense)                                    |                                               | -                                                      | 330                                                    | 330                     |                                                                                                                                                                   |
| 32 Taxes: Property Taxes                                     |                                               | -                                                      | -                                                      | -                       |                                                                                                                                                                   |
| 33 Taxes: State & Local Use Tax                              |                                               | (23,131)                                               | (20,148)                                               | 2,983                   |                                                                                                                                                                   |
| 34 Other Non-operating margins                               |                                               | -                                                      | -                                                      | -                       |                                                                                                                                                                   |
| 35 TOTAL NON-OPERATING MARGINS (EXPENSE)                     | (46,263)                                      | (23,131)                                               | (19,661)                                               | 3,470                   |                                                                                                                                                                   |
| 36 Federal Income Tax Expense                                | -                                             | -                                                      | -                                                      | -                       |                                                                                                                                                                   |
| 37 GRAND TOTAL NET MARGIN DETAIL BREAKOUT                    | (1,165,462)                                   | (738,121)                                              | (522,392)                                              | 215,729                 |                                                                                                                                                                   |
|                                                              |                                               |                                                        |                                                        |                         |                                                                                                                                                                   |
| Total Net Margin                                             | \$ (1,165,462)                                | \$ (738,121)                                           | \$ (522,392)                                           | \$ 215,729              | Risk Model in line with expectations (RI transaction & Deployment Speed)                                                                                          |

# ISLAND NETWORK

## BALANCE SHEET

|                                                  | A.                                             | B.                                             |                                 |
|--------------------------------------------------|------------------------------------------------|------------------------------------------------|---------------------------------|
|                                                  | Island Network Actual<br>Period End<br>3/31/15 | Island Network Actual<br>Period End<br>6/30/15 |                                 |
| <b>1 ASSETS</b>                                  |                                                |                                                |                                 |
| 2 Current Assets                                 |                                                |                                                |                                 |
| 3 Cash                                           | \$ 671,025                                     | \$ 745,761                                     |                                 |
| 4 Accounts Receivable                            | 60,519                                         | 67,561                                         |                                 |
| 5 Inventory                                      | 115,393                                        | 121,902                                        |                                 |
| 6 Prepays And Other Current Assets               | 19,107                                         | 28,057                                         |                                 |
| 7 <b>Total Current Assets</b>                    | <b>866,045</b>                                 | <b>963,280</b>                                 |                                 |
| <b>8 PROPERTY, PLANT, AND EQUIPMENT</b>          |                                                |                                                |                                 |
| 9 Fixed Assets                                   | 1,534,364                                      | 2,560,579                                      |                                 |
| 10 Accumulated Depreciation                      | (1,128,988)                                    | (1,160,175)                                    |                                 |
| 11 <b>Total Property &amp; Equipment - Other</b> | <b>405,375</b>                                 | <b>1,400,404</b>                               |                                 |
| 12 Investments in Affiliated Co.                 | 900,000                                        | 707,731                                        | Fine tuning acquisition figures |
| 13 Other assets                                  | -                                              | -                                              |                                 |
| 14 Goodwill                                      | 352,050                                        | 544,319                                        | Fine tuning acquisition figures |
| 15 <b>Total Assets</b>                           | <b>2,523,470</b>                               | <b>3,615,734</b>                               |                                 |
| 16                                               |                                                |                                                |                                 |
| <b>17 CURRENT LIABILITIES</b>                    |                                                |                                                |                                 |
| 18 Accounts Payable                              | 395,667                                        | 24,774                                         |                                 |
| 19 Other Payables                                | 92,949                                         | 91,967                                         |                                 |
| 20 <b>Total Current Liabilities</b>              | <b>488,616</b>                                 | <b>116,742</b>                                 |                                 |
| <b>21 NONCURRENT LIABILITIES</b>                 |                                                |                                                |                                 |
| 22 Long-term Debt Startup Capital (OPALCO)       | 1,548,579                                      | 2,876,943                                      |                                 |
| 23 Long-term Obligation on Leased Equipment      | -                                              | 454,431                                        |                                 |
| 24 <b>Total Liabilities</b>                      | <b>2,037,195</b>                               | <b>3,448,115</b>                               |                                 |
| 25                                               |                                                |                                                |                                 |
| <b>26 EQUITIES AND MARGINS</b>                   |                                                |                                                |                                 |
| 27 Common Stock                                  | 10,000                                         | 10,000                                         |                                 |
| 28 Preferred Stock                               | 100                                            | 100                                            |                                 |
| 29 Retained Earnings                             | 679,912                                        | 679,912                                        |                                 |
| 30 Net Income (Loss)                             | (203,737)                                      | (522,392)                                      |                                 |
| 31 <b>Total Equity</b>                           | <b>486,275</b>                                 | <b>167,620</b>                                 |                                 |
| 32 <b>Total Liabilities and Equity</b>           | <b>\$ 2,523,470</b>                            | <b>\$ 3,615,734</b>                            |                                 |

**ISLAND NETWORK  
STATEMENT OF CASH FLOW  
NON GAAP**

|                                                               | <b>A.<br/>2015<br/>Island Network<br/>Updated Annual<br/>Budget</b> | <b>B.<br/>Actual<br/>Island Network<br/>Period End<br/>6/30/2015</b> |
|---------------------------------------------------------------|---------------------------------------------------------------------|----------------------------------------------------------------------|
| 1 OPERATING ACTIVITIES                                        |                                                                     |                                                                      |
| 2 Margins                                                     | \$ (1,165,000)                                                      | \$ (522,392)                                                         |
| 3 Depreciation/Amortization                                   | 245,000                                                             | 25,647                                                               |
| Adjustments to reconcile net earnings to net cash             |                                                                     |                                                                      |
| 4 provided/(used) by operating activities:                    |                                                                     |                                                                      |
| 5 Change in Inventory                                         | -                                                                   | (121,902)                                                            |
| 6 Change in Accounts Receivable                               | -                                                                   | (22,835)                                                             |
| 7 Change in Prepaids and Other Current Assets                 | -                                                                   | (21,797)                                                             |
| 8 Change in Accounts Payable                                  | -                                                                   | (318,523)                                                            |
| 9 Change in Other Current and Noncurrent Liabilities          | -                                                                   | 89,301                                                               |
| 10 Cash Flow Operations                                       | <b>(920,000)</b>                                                    | <b>\$ (892,502)</b>                                                  |
| 11                                                            |                                                                     |                                                                      |
| 12 PLANT INVESTMENT (NET)                                     |                                                                     |                                                                      |
| 13 Investment in affiliate, net of cash acquired <sup>1</sup> | -                                                                   | (707,731)                                                            |
| 14 Purchases of property and equipment                        | (2,050,000)                                                         | (530,948)                                                            |
| 15 Cash Flow From Operations and Plant Investment             | <b>(2,970,000)</b>                                                  | <b>(2,131,181)</b>                                                   |
| 16 Cash Flow Before Borrowing                                 | (2,970,000)                                                         | (2,131,181)                                                          |
| 17                                                            |                                                                     |                                                                      |
| 18 NET BORROWING                                              |                                                                     |                                                                      |
| 19 Debt borrowings, net                                       | 2,641,000                                                           | 2,876,943                                                            |
| 20 Cash Increase (Decrease) After Net Borrowing               | <b>(329,000)</b>                                                    | <b>745,761</b>                                                       |
| 21                                                            |                                                                     |                                                                      |
| 22 TOTAL OUTSTANDING DEBT BALANCE <sup>1</sup>                | <b>\$ (2,641,000)</b>                                               | <b>\$ (2,876,943)</b>                                                |
| 23                                                            |                                                                     |                                                                      |
| 24 NOTE: 1. Excludes Rock Island Purchase                     |                                                                     |                                                                      |