

MEMORANDUM

March 11, 2016

To: Board of Directors

From: Foster Hildreth, General Manager

Re: 2015 Year End Unaudited Financial Report for Rock Island Communications

Please see attached the 2015 Year-end Unaudited Financial Report for Rock Island Communications. Included in the report package are the Income Statement, Balance Sheet and Statement of Cash Flows.

Operating revenue for the year was down compared to budget (\$423k) and operating expenses were over (\$500k). These variances were due, for the most part, to a shift in direction and design when T-Mobile came onboard. The short term revenue delay is more than offset by the long term benefits this arrangement provides. The T-Mobile arrangement provides a low cost, rapidly deployable, countywide solution for our LTE network. The shift required us to retool our designs, it accelerated the scope and timeline of our plans, and it delayed bringing LTE subscribers onboard. In summary, the total net loss was larger than budgeted by \$665k.

The total subscriber count was close to target on the fiber side (489 out of 500 subscribers) but fell short on the LTE side (39 out of 608 subscribers) because of delays when we retooled our plans with T-Mobile. For 2016, the pipeline for fiber subscribers is already full and LTE deployment is ramping up. Since January 1st, 11 active LTE poles have been deployed and 31 of the 38 poles will be active by year end, more than compensating for the subscriber delay in 2015.

Key lessons learned in 2015 include:

- In order to provide the level of service that we expect, we needed more staff to keep up with the high volume of member requests.
- We have now worked out permit processes with the county to streamline the (archeological, CAO, joint use wireless, and public works) challenges as experienced in 2015.
- The partnership with T-Mobile, although initially complex, allowed for a reduction in the number of LTE pole sites. Those sites allow for coverage throughout most of our service territory by year end 2016. These LTE capabilities and service levels have exceeded expectations.
- Navigating through the dynamic relationship between a for-profit subsidiary and a non-profit cooperative.

For more detail, please note the following key points from our year of start-up operations:

- We started 2015 as Island Network, LLC with a goal of building a hybrid fiber and LTE system to serve about 25% of the county, in order to reach a financial break-even point.
- On February 6, 2015, we acquired Rock Island Technology Solutions. We merged operations, hired employees and shifted our plans as a new organization, Rock Island Communications.
- We entered into a partnership with T-Mobile that brought a more robust solution which allowed for a broader deployment and enhanced service levels.
- The T-Mobile agreement reduced the total number of poles required to complete deployment from 120 to 38, but required us to accelerate deployment by year-end 2016 from the 6 LTE poles planned to 31. With T-Mobile on board, services will be available to most of San Juan County by year-end 2016, compared to 25% of the County in the “go it alone” plan.

Rock Island Communications 2015 Year-End Unaudited Financial Report





Balance Sheet

	A. Island Network Department Audited 12/31/14	B. Unaudited Rock Island 12/31/2015
1 ASSETS		
2 Current Assets		
3 Cash	-	225,976
4 Accounts Receivable	45,473	89,876
5 Inventory	-	1,642,206
6 Prepaid And Other Current Assets	5,512	9,583
7 Total Current Assets	50,985	1,967,641
8 PROPERTY, PLANT, AND EQUIPMENT		
9 Fixed Assets	165,436	4,613,008
10 Accumulated Depreciation	(90,545)	(1,262,651)
11 Total Property & Equipment	74,891	3,350,357
12 Investments in Affiliated Co.	-	-
13 Other assets	-	3,600
14 Goodwill	-	282,257
15 Total Assets	125,876	5,603,854
16		
17 CURRENT LIABILITIES		
18 Accounts Payable	-	287,298
19 Other Payables	2,667	117,384
20 Total Current Liabilities	2,667	404,682
21 NONCURRENT LIABILITIES		
22 Long-term Debt Startup Capital (OPALCO)	343,297	7,029,993
23 Total Liabilities	345,964	7,434,675
24		
25 EQUITIES AND MARGINS		
26 Retained Earnings	(220,088)	-
27 Net Income (Loss)		(1,830,821)
28 Total Equity	(220,088)	(1,830,821)
29 Total Liabilities and Equity	125,876	5,603,854



Income Statement

	A.	B.	C.	D.
	Budget	Unaudited		
	Period End	Period End	Variance	
	12/31/2015	12/31/2015	(B-A)	Comments
I OPERATING REVENUES				
1 Sales	2,253,168	1,829,350	(423,818)	Primarily LTE rollout delay due to T-Mobile re-tooling
2 TOTAL OPERATING REVENUES	2,253,168	1,829,350	(423,818)	
3				
4 II COST OF GOODS SOLD	967,174	777,451	(189,723)	Less sales than budgeted
5 TOTAL COST OF GOODS SOLD	967,174	777,451	(189,723)	
6 Gross Profit	1,285,994	1,051,899	(234,095)	
7 III OPERATING EXPENSES				
8 Advertising	75,000	57,297	(17,703)	
9 Depreciation/Amortization Expense	225,056	126,529	(98,527)	Less expense due to delays in capital project completion
10 Insurance	100,000	114,217	14,217	
11 Office Expenses	-	313,808	313,808	Originally budgeted in other line items. Includes expenses for start-up, office sup.= \$60k & costs transitioned from the OPALCO IN department
12 Payroll Expenses	1,325,138	1,308,842	(16,296)	
13 Professional Fees	200,000	600,270	400,270	Due to T-Mobile strategic re-direction, consultant scope increased
14 Rent	120,000	130,014	10,014	
15 Utilities	130,000	10,696	(119,304)	Budgeted costs hitting other operating expenses above
16 Other	-	800	800	
17 Travel & Ent	20,000	35,141	15,141	
18 TOTAL OPERATING EXPENSES	2,195,193	2,697,613	502,420	
19 TOTAL NET OPERATING MARGINS	(909,199)	(1,645,714)	(736,514)	
20 IV OTHER INCOME (EXPENSE)				
21 Interest Income	-	327	327	
22 Other Income (Expense)	-	2,820	2,820	
23 Taxes: State & Local Use Tax	(46,263)	(59,238)	(12,976)	
24 Other Income - Parent	-	29,100	29,100	Charge to OPALCO for network management services - per IRS guidelines
25 Interest Expense	(36,000)	-	36,000	No third party borrowings
26 Interest Expense - Parent	(174,000)	(99,822)	74,178	Less interest charge from OPALCO than budgeted due to lower interest rates
27 Other expense - Parent	-	(58,294)	(58,294)	OPALCO charge for use of backbone - per IRS guidelines
28 TOTAL OTHER INCOME	(256,263)	(185,107)	71,156	
29 Federal Income Tax Expense	-	-	-	No federal tax for these years (net operating loss)
30 GRAND TOTAL NET MARGIN DETAIL BREAKOUT	(1,165,462)	(1,830,821)	(665,358)	



Statement of Cash Flows

	Period Ended December 31, 2015
Cash Flows from Operating Activities:	
1 Net income (loss)	(1,830,821)
2 Adjustments to reconcile net income (loss) to net cash	
3 provided by (used in) operating activities	
4 Depreciation/Amortization	126,529
5 Changes in assets and liabilities:	
6 Accounts receivable	(20,918)
7 Inventory	(1,568,061)
8 Prepaid and other assets	190,505
9 Accounts payable	256,424
10 Accrued and other liabilities	84,109
11	
12 Net cash provided by (used in) operations:	(2,762,233)
13	
14 Cash Flows from Investing Activities:	
15 Additions to property and equipment, net	(3,293,191)
16 Acquisition of Rock Island assets and liabilities, net (Note 1)	(625,384)
18 Net cash provided by (used in) investing activities:	(3,918,574)
19	
20 Cash Flows from Financing Activities:	
21 Proceeds from debt (OPALCO), net (Note 2 & 3)	6,906,783
22 Net cash provided by (used in) financing activities:	6,906,783
23	
24 Net change in cash	225,976
25	
26 Cash and cash equivalents, beginning of period	-
27 Cash and cash equivalents, end of period	225,976
28	
29 Notes:	
30 1 Consists of assets acquired of \$376,125 - liabilities acquired (\$112,365) + purchase price goodwill \$361,624.	
31 2 Consists of: IN LLC funding (pre-Rock Island) \$1,350,275 + transition of IN department assets/liabilities \$639,343 + start-up funding to RIC \$4,917,165	
32 3 \$7.5million Rock Island start-up: \$4,917,165 (2015) + \$2,600,000 (2016) = \$7,517,165	