Confidential per WAC 480-07-160

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

Audited Consolidated Financial Statements

December 31, 2014 and 2013

REDACTED

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

Audited Consolidated Financial Statements

December 31, 2014 and 2013

Johnson Stone & Pagano, P.S.
Certified Public Accountants
1501 Regents Blvd., Suite 100
Fircrest, WA 98466-6060

Independent Auditor's Report

To the Board of Directors
Whidbey Telephone Company
Langley, Washington

Report on the Financial Statements

We have audited the accompanying consolidated financial statements of Whidbey Telephone Company and Subsidiaries which comprise the consolidated balance sheets as of December 31, 2014 and 2013, and the related consolidated statements of income and comprehensive income, stockholders' equity and cash flows for the years then ended, and the related notes to the consolidated financial statements.

Management's Responsibility for the 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 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. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of 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 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 the 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 opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Whidbey Telephone Company and Subsidiaries as of December 31, 2014 and 2013, and the results of its operations and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Johnson, Stone & Pagano, P.S.

JOHNSON, STONE & PAGANO, P.S.

April 29, 2015

AUDITED CONSOLIDATED FINANCIAL STATEMENTS

Confidential per WAC 480-07-160

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

December 31, 2014 and 2013

	2014	2013
ASSETS	[redacted]	
CURRENT ASSETS		
Cash and cash equivalents (Notes 1 and 2)		
Accounts receivable		
Trade (Notes 1, 2 and 3)		
Other (Note 10)		
Materials and supplies (Note 1)		
Prepayments and deposits		
Total Current Assets		
OTHER ASSETS		
Investments (Notes 1, 2 and 4)		
Total Other Assets		
PROPERTY, PLANT AND EQUIPMENT (Notes 1, 5 and 11)		
Telecommunications plant in service		
Less allowances for depreciation		
Telecommunications plant under construction		
Plant held for future use		
Total Telecommunications Plant		
Nonregulated plant		
Less allowances for depreciation		
Nonregulated plant under construction		
Total Nonregulated Plant		
TOTAL ASSETS		

The accompanying notes are an integral part of these consolidated financial statements.

REDACTED

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS (Continued)

December 31, 2014 and 2013

	2014	2013
LIABILITIES AND STOCKHOLDERS' EQUITY	[redacted]	
CURRENT LIABILITIES		
Accounts payable		
Taxes, other than income taxes		
Other current liabilities		
Deferred revenue (Note 1)		
Current portion of long-term debt (Note 6)		
Total Current Liabilities		
LONG-TERM DEBT, less portion classified as a current liability (Note 6)		
Total Liabilities		
STOCKHOLDERS' EQUITY		
Capital stock (Note 7)		
Retained earnings		
Accumulated other comprehensive income		
Total Stockholders' Equity		
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY		

The accompanying notes are an integral part of these consolidated financial statements.

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

Years Ended December 31, 2014 and 2013

	2014	2013
OPERATING REVENUES (Note 1)	[redacted]	
Local network service revenues		
Network access service revenues		
Long distance network service revenues		
Other operating revenues		
Uncollectible revenues (deduction)		
Total Operating Revenues		
OPERATING EXPENSES		
Plant specific operations		
Plant nonspecific operations		
Depreciation and amortization		
Customer operations		
Corporate operations		
Taxes, other than income taxes		
Total Operating Expenses		
Net Operating Loss		
OTHER INCOME, EXPENSE AND TAXES - NET		
Other income		
Income (Loss) Available for Fixed Charges		
FIXED CHARGES AND RELATED ITEMS - NET		
NET INCOME (LOSS)		
OTHER COMPREHENSIVE INCOME (LOSS)		
Unrealized gain (loss) on investments		
COMPREHENSIVE INCOME (LOSS)		

The accompanying notes are an integral part of these consolidated financial statements.

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Confidential per WAC 480-07-160

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

Years Ended December 31, 2014 and 2013

	Capital Stock	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
BALANCE AT DECEMBER 31, 2012	[redacted]			
Distributions to stockholders				
Net loss for the year				
Other comprehensive loss				
BALANCE AT DECEMBER 31, 2013				
Distributions to stockholders				
Net income for the year				
Other comprehensive income				
BALANCE AT DECEMBER 31, 2014				

The accompanying notes are an integral part of these consolidated financial statements.

REDACTED

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years Ended December 31, 2014 and 2013

	2014	2013
CASH FLOWS FROM OPERATING ACTIVITIES	[redacted]	
Cash received from customers and settlements		
Cash paid to vendors, suppliers and employees		
Interest and dividends received		
Interest paid		
Net Cash Provided (Used) by Operating Activities		
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to property, plant and equipment		
Salvage on retired property, plant and equipment		
Partnership capital distribution		
Proceeds from sale of investments		
Purchase of investments		
Net Cash Provided (Used) by Investing Activities		
CASH FLOWS FROM FINANCING ACTIVITIES		
Distributions to stockholders		
Proceeds from long-term debt		
Payments on long-term debt		
Net Cash Used by Financing Activities		
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS		
Cash and Cash Equivalents at Beginning of Year		
CASH AND CASH EQUIVALENTS AT END OF YEAR		

The accompanying notes are an integral part of these consolidated financial statements.

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)

Years Ended December 31, 2014 and 2013

	2014	2013
RECONCILIATION OF NET INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	[redacted]	
Net income (loss)		
Adjustments to reconcile net income (loss) to net cash provided (used) by operating activities		
Depreciation and amortization		
Partnership distribution included in net income and not included in operating activities		
Realized gain on sale of investments		
Noncash operating income		
(Increase) decrease in assets		
Accounts receivable		
Materials and supplies		
Prepayments and deposits		
Increase (decrease) in liabilities		
Accounts payable		
Taxes, other than income taxes		
Other current liabilities		
Deferred revenue		
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES		

The accompanying notes are an integral part of these consolidated financial statements.

REDACTED

NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation
The consolidated financial statements include the accounts of Whidbey Telephone Company (the "Company") and its wholly-owned subsidiaries, Western Long Distance, Inc., American Alarm Systems, Inc., FiberCloud, Inc., WaterCrest, Inc., Second Wind at Ten, LLC and WiFire, Inc. (collectively, "Company and Subsidiaries"). All material intercompany accounts and transactions have been eliminated in consolidation.

Organization and Regulation
The Company is a local exchange telecommunications company. The Company, together with its subsidiary Western Long Distance, Inc., provides local exchange, long distance and other telecommunications services including digital subscriber lines to South Whidbey Island and Point Roberts, Washington. The Company also provides internet access services and web-hosting services to customers in western Washington, located both within and outside its local exchange service areas. American Alarm Systems, Inc. provides alarm system installation and alarm monitoring services in western Washington. FiberCloud, Inc. provides offsite computer data storage, hosted services, internet access and web-hosting services in western Washington (see Note 11). WaterCrest, Inc. and its wholly-owned subsidiary, Second Wind at Ten, LLC, are real estate development companies with a primary focus in western Washington. WiFire, Inc. is a coffee bar located in Freeland, Washington. The Company and each of its subsidiaries are organized under the laws of the State of Washington.

The Company is a small rate-of-return carrier. The Federal Communication Commission ("FCC") Report and Order and Further Notice of Proposed Rulemaking, ("FCC 11-161"), reformed the universal service and intercarrier compensation systems. These reforms modify the manner in which the Company recovers its telecommunications revenue requirements.

Accounting Records
Accounting records are maintained in accordance with the Uniform System of Accounts ("USOA") prescribed by the Federal Communications Commission ("FCC") and, to the extent permitted by the USOA, accounting principles generally accepted in the United States of America. The accounting methods observed by the Company for book and recording purposes are subject to the concurrence of the Washington Utilities and Transportation Commission ("WUTC").

Cash and Cash Equivalents
The Company and Subsidiaries consider all highly liquid debt instruments to be cash equivalents.

Materials and Supplies
Materials and supplies are stated at average cost.

NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Investments
Investments are stated at market value if readily determinable or at cost.

Fair Value Measurements
The Company provides information regarding the inputs that underlie a fair value measurement of financial instruments. The three levels of inputs essentially distinguish the relative reliability of inputs to fair value measurements. Level 1 inputs are more reliable and objective than Level 2 inputs which are in turn more reliable and objective than Level 3 inputs. In arriving at a fair value measure, the Company is required to determine the level in the fair value hierarchy within which a fair value measurement ultimately falls and provide disclosure of such determinations (see Note 4).

Accounting for Long-Lived Assets
The Company and Subsidiaries periodically review long-lived assets such as property, plant and equipment for potential impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. At December 31, 2014, management has determined that there were no material impairment charges to be recorded as of that date.

Regulated Telecommunications Plant, Maintenance and Depreciation
Regulated telecommunications plant is stated at original cost. The cost of additions to plant includes contracted work, direct labor, materials and overhead. When units of property are retired, the original cost plus removal costs, less salvage, is charged to accumulated depreciation with no gain or loss recognized. The costs of normal maintenance and repairs are charged to operating expense. Depreciation is computed using the straight-line method for financial reporting and accelerated methods for income tax purposes (see Note 5).

Revenue Recognition, Major Customers and Services
Services provided by the Company and Subsidiaries include local network, long distance network and network access services, as well as other services. In the normal course of business of the Company and Subsidiaries, certain long distance network and network access service revenues are subject to out-of-period adjustments. Such adjustments are normal occurrences and are recorded by the Company and Subsidiaries during the year in which they become determinable.

Network access service revenues, which represent a major portion of the Company's operating revenues, are derived from the provision of exchange access services to interexchange carriers or to end users of telecommunication services.

NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition, Major Customers and Services *(Continued)*
The FCC 11-161 modified and replaced the existing system with universal service reform and intercarrier compensation reform. A Connect America Fund has been established to replace all existing high-cost support mechanisms and sets broadband service requirements. Alongside the broadband service rules, reforms to establish a framework to limit reimbursements for excessive capital and operating expenses have been implemented as of July 1, 2012 and phase outs of certain support payments have occurred. Intercarrier compensation reform adopts a uniform bill-and-keep framework as the ultimate end state for all telecommunications traffic exchanged with the Company. Intercarrier compensation rates are capped and the disparity between intrastate and interstate terminating end office rates are being brought to parity in two steps as outlined in FCC 11-161. The state's public utilities commissions will be overseeing the modifications to rates in intrastate tariffs. Limits on carriers' total eligible recovery will reflect existing downward trends on intercarrier compensation revenues with declining switching costs and minutes of use.

The Company continues to review the reforms and modifications to the support that the Company receives and understands that those reforms and modifications could have an adverse effect on the Company's revenues and cash flow. Revenue impacts are subject to change based upon future data collections and further clarification from the FCC.

Revenues for intrastate access services are received through tariffed access charges filed by the Company at the WUTC. Once filed, the tariffed access charges become effective if specifically approved by the WUTC or allowed to become effective by operation of law. The intrastate switched access charges are billed by the Company to intrastate interexchange carriers. Intrastate special access charges are also billed to intrastate interexchange carriers that order such services and, in some cases, to retail customers that order special access services. Before July 1, 2014, the switched access charges associated with carrier common line and state universal service fund were pooled with all Washington Exchange Carrier Association ("WECA") member companies and the Company received a distribution of net revenues based upon the Company's proportionate share of WUTC approved revenue objectives of all participating WECA member companies.

Effective July 1, 2014, the WUTC implemented a state universal communications service program ("State USF Program") that temporarily replaced the terminated universal service support pool ("Traditional USF") administered by WECA and also replaced the cumulative reduction in support the Company received from the federal Connect America Fund ("CAF"). The State USF Program was to begin January 2015 which resulted in a cash flow issue for some of the companies that met the WUTC criteria to be eligible for such support. The WUTC granted a one-time partial distribution in 2014 of the State USF Program equal to the amount the Company received from the Traditional USF for 2012 in the amount of $[redacted]. The remainder of the annual distribution, which was comprised of the cumulative reduction in CAF support of $[redacted], was disbursed in January 2015. Subsequent annual disbursements

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2014 and 2013

NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Revenue Recognition, Major Customers and Services *(Continued)*
comprised of the Traditional USF and the disbursement of the cumulative CAF deficit support are scheduled to occur in January of the following State USF Program years, assuming the Company continues to be eligible under the program. The State USF Program year runs from July 1 to June 30, therefore, the Company accrued $[redacted] as a receivable due from the State USF Program for the period July 1, 2014 to June 30, 2015, and deferred revenue of $[redacted] for the unearned portion. The State USF Program is scheduled to last for five program years.

As of July 31, 2014, WECA terminated the pooling of originating carrier common line ("CCL") minutes of use and the Company opted to keep its existing originating CCL rate, which was allowed by the WUTC to become effective as a matter of law.

For some of the services that the Company and Subsidiaries provide to their respective customers, the Company and Subsidiaries rely upon services and facilities supplied to the Company and Subsidiaries by other companies. Any material disruption of the services or facilities supplied to the Company and Subsidiaries by other companies could potentially have an adverse effect upon the operating results of the Company and Subsidiaries.

Federal Income Taxes
Effective January 1, 2005, the Company elected to become a Subchapter S corporation and elected to have each of its then-existing and subsequently formed subsidiaries to be Qualified Subchapter S Subsidiaries. Similar elections were made for WaterCrest, Inc. and WiFire, Inc. on the dates of their incorporations. Second Wind at Ten, LLC is organized as a single member LLC, as such, its activities flow through to its sole member, Watercrest, Inc. Taxable earnings and losses of the Company and its subsidiaries on and after that date are included in the consolidated tax return of the Company, amounts from which are then included in the tax return of the Company's stockholders and taxed at the applicable tax rate of the stockholders.

The Company's federal income tax returns for the tax years ending before December 31, 2011 are closed to examination.

Use of Estimates
The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure 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 may differ from those estimates and assumptions used in preparing the accompanying financial statements.

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2014 and 2013

NOTE 1 - NATURE OF OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Subsequent Events
The management of the Company evaluated for subsequent events and transactions for potential recognition and disclosure through April 29, 2015, the date the financial statements were available to be issued. All identified material events or transactions have been recorded or disclosed (see Note 11).

NOTE 2 - CONCENTRATION OF CREDIT RISK

The Company and Subsidiaries maintain cash balances at various financial institutions in western Washington. Accounts at each of the financial institutions are insured by the Federal Deposit Insurance Corporation ("FDIC") with basic coverage up to $250,000. The Company and its subsidiaries periodically maintain cash in excess of federally insured limits. At December 31, 2014, the Company and its subsidiaries' cash balances exceeded the insured amount by $[redacted].

The Company has an account with a broker-dealer with investments including a money market fund and certain securities. Securities held at such institutions are each insured by the Securities Investor Protection Corporation up to $500,000 for brokerage accounts, of which $250,000 of the total available applies to any cash claims. The balance in the money market fund at December 31, 2014 is $[redacted].

The Company's accounts receivable are subject to potential credit risk as they are unsecured.

NOTE 3 - ACCOUNTS RECEIVABLE

The trade accounts receivable balances at December 31, 2014 and 2013 consist of:

	2014	2013
Accounts receivable - subscribers	[redacted]	
Accounts receivable - interexchange carriers and exchange carrier associations		
Allowance for doubtful accounts (deduction)		

REDACTED

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2014 and 2013

NOTE 3 - ACCOUNTS RECEIVABLE (Continued)

The Company and Subsidiaries extend credit to business and residential customers based upon a written credit policy. Service interruption is the primary vehicle for controlling accounts receivable losses. Telecommunications accounts receivable are recorded when subscriber bills, carrier access bills and exchange carrier associations settlement statements are rendered and are reflected in the balance sheets net of the allowance for doubtful accounts. Certain exchange carrier associations' settlements are subject to out-of-period adjustments. Such settlements and adjustments are recorded during the year in which they become determinable. The allowance for doubtful accounts is estimated based on the Company's historical uncollectibles, the existing economic conditions in the telecommunications industry and the financial stability of its customers. As of December 31, 2014, approximately [redacted]% of accounts receivable were outstanding ninety days or more after the date of the invoice on which they were first billed.

NOTE 4 - INVESTMENTS

Investments consist of:

	2014	2013
Investments at fair value	[redacted]	
Verizon Communications, Inc.		
Sun Life Financial Services of Canada, Inc.		
Frontier Communications		
Mutual funds held at Edward Jones		
Associated Network Partners, Inc.		
Western Independent Networks		
Artifact Technologies, Inc.		
Investments at cost		
Personal Communications Services ("PCS") licenses and 700 MHz Licenses		
Note receivable - Green Tea Northwest, LLC		
Notes receivable - stockholders		
Land held for investment		

During 2014, the Company sold its remaining PCS 700 MHz licenses.

NOTE 4 - INVESTMENTS (Continued)

During 2005, Green Tea Northwest, LLC borrowed $[redacted] from WaterCrest, Inc. Accrued interest on the note in the amount of $[redacted] and $[redacted] was added to the note with total accrued interest on the note of $[redacted] and $[redacted] in 2014 and 2013, respectively. This borrowing is evidenced by a promissory note and is subject to the terms stated therein. The note bore interest at [redacted]% per annum and was to be paid in full by November 3, 2010. During November 2010, the note was renegotiated with interest at [redacted]% per annum, due November 3, 2015, with a beginning principal balance of $[redacted]. A stockholder of the Company is a member of Green Tea Northwest, LLC.

Also included in investments are notes receivable from two stockholders of the Company issued in 2014 for $[redacted] and 2013 for $[redacted], each. These notes total $[redacted] for 2014 and $[redacted] for 2013. The notes receivable are evidenced by various promissory notes and are subject to the terms stated therein. These notes bear interest ranging from [redacted]% to [redacted]% per annum, and are unsecured. Interest accrued through December 31, 2014 and 2013 on such notes was $[redacted] and $[redacted], each, respectively and will be added to the balances per the terms of the notes. The Company also has a note receivable from three trusts, in equal amounts, of whom the trustees are stockholders for $[redacted] and $[redacted] at December 31, 2014 and 2013, respectively. The note is evidenced by a promissory note and is subject to the terms stated therein. The note bears interest at the AFR in effect at the time advances were made on the note, and is unsecured. The interest ranges from [redacted]% to [redacted]% per annum.

The Company has a [redacted] share of Series A stock ([redacted]% aggregate interest) in Artifact Technologies, Inc., a company organized to conduct an internet-based business.

Assets measured at fair value on a recurring basis at December 31, 2014 and 2013 are as follows:

		Fair Value Measurements		
	Fair Value	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Other Subjective Inputs (Level 3)
December 31, 2014				
Verizon Communications, Inc.	[redacted]			
Sun Life Financial Services of Canada, Inc.				
Frontier Communications				
Growth and Income mutual funds held at Edward Jones				
Associated Network Partners, Inc.				
Western Independent Networks				
Artifact Technologies, Inc.				

NOTE 4 - INVESTMENTS (Continued)

		Fair Value Measurements		
	Fair Value	Quoted Prices in Active Markets For Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Other Subjective Inputs (Level 3)
December 31, 2013	[redacted]			
Verizon Communications, Inc.				
Sun Life Financial Services of Canada, Inc.				
Frontier Communications				
Growth and Income mutual funds held at Edward Jones				
Associated Network Partners, Inc.				
Western Independent Networks				
Artifact Technologies, Inc.				

Investments valued using Level 1 inputs are based on unadjusted quoted market prices within active markets. Investments valued using Level 2 inputs are based primarily on quoted prices for similar assets in active or inactive markets. Level 3 inputs are based on the Company's own assumptions on how knowledgeable parties would price assets or liabilities and are developed using the best information available in the circumstances.

The Company holds a limited partnership interest in Seattle SMSA Limited Partnership ("Partnership"); the investment is carried at cost with no basis for financial statement purposes as the cumulative distributions received exceed the capital contributed. Management has determined there are no identified events or changes in circumstances that would have a significant adverse effect on the fair value of the investment. The Company has not made fair value disclosures for its interest as management has further determined that it is not practicable to estimate the fair value of the investment as the Company holds a less than [redacted]% interest in the Partnership, the cost to determine the fair value would be prohibitive and the financial information of the Partnership is proprietary among the Company and the partners. The Company's capital account in the Partnership at December 31, 2014 and 2013 was $[redacted] and $[redacted], respectively. During the years ended December 31, 2014 and 2013, the Company received partnership distributions of $[redacted] and $[redacted], respectively which are included in other income for 2014 and 2013 in the Consolidated Statements of Income.

NOTE 5 - PROPERTY, PLANT AND EQUIPMENT AND DEPRECIATION
(See Note 1)

Regulated Telecommunications Plant
As required by the USOA, telecommunications plant is stated at its original cost, when first devoted to public service.

Major classes of the telecommunications plant assets in service as of December 31, 2014 and 2013 are:

	2014	2013
General support facilities	[redacted]	
Central office equipment		
Cable and wire facilities		

Provision has been made for depreciation of the major classes of the telecommunications plant in service at straight-line annual rates as follows:

General support facilities	[redacted]
Buildings	
Furniture and office equipment	
Vehicles and other work equipment	
Central office equipment	
Radio systems	
Other	
Cable and wire facilities	

Nonregulated Plant
Nonregulated plant is recorded at original cost when first placed in service. The Company and Subsidiaries provide for depreciation using the straight-line method at annual rates which are intended to amortize the depreciable property over its estimated useful life. The depreciable lives range from 5 to 25 years.

WHIDBEY TELEPHONE COMPANY AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2014 and 2013

NOTE 5 - PROPERTY, PLANT AND EQUIPMENT AND DEPRECIATION
(See Note 1) (Continued)

Depreciation Expense
The provision for depreciation on regulated telecommunications plant and nonregulated plant in service is:

	2014	2013
Regulated telecommunications plant	[redacted]	
Nonregulated plant		

NOTE 6 - NOTES PAYABLE AND LONG-TERM DEBT

Notes payable and long-term debt at December 31, 2014 and 2013 consists of the following:

	2014	2013
Note payable consists of a revolving reducing line of credit with Wells Fargo Bank of up to a maximum of $[redacted] at December 31, 2014 reduced each quarter by payments of $[redacted] beginning June 2013. The agreement calls for monthly payments of interest at [redacted]% above a daily one month LIBOR rate as determined by the bank, with interest rate selection options available to the Company ([redacted]% at December 31, 2014 and 2013). Principal and accrued interest are due June 21, 2015. Security includes all assets as noted in the security agreement.	[redacted]	
Note payable consists of a revolving line of credit with Wells Fargo Bank of up to a maximum of $[redacted]. The agreement calls for monthly payments of interest at [redacted]% above a daily one month LIBOR rate as determined by the bank with interest selection options available to the Company ([redacted]% at December 31, 2014 and 2013). Principal and accrued interest are due June 21, 2015. Security includes all assets as noted in the security agreement.		

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NOTE 6 - NOTES PAYABLE AND LONG-TERM DEBT (Continued)

	2014	2013
Less portion due within one year classified as a current liability	[redacted]	
Long-term Debt		

Aggregate annual maturities of long-term debt, which are expected to be renegotiated with similar terms and repayment schedule before the June 2015 renewal date for the next four years are as follows:

2015	[redacted]
2016	
2017	
2018	

As part of the promissory notes and agreements executed by the Company with respect to the notes payable, the Company agreed to various negative covenants including limitations on additions to fixed assets, annual lease payments, guarantees, other indebtedness, loan advances and investments. The Company also agreed to comply with certain financial covenants as a condition to each of the credit facilities. The Company was in compliance at December 31, 2014.

NOTE 7 - CAPITAL STOCK

The authorized, issued and outstanding shares for the years ended December 31, 2014 and 2013 are as follows:

	Shares		Stated Capital
	Authorized	Issued	Value
Common stock - no par, voting	[redacted]		
Common stock - no par, non-voting			

REDACTED

NOTE 8 - LEASES AND SERVICE AGREEMENTS

FiberCloud, Inc. ("FiberCloud") assumed a lease agreement for leased office space in Everett, Washington effective December 30, 2009. The term of the agreement is for ten years. As defined in the agreement, base rent can be increased by the scheduled amounts as noted in the agreement and FiberCloud's prorata share of reasonable and customary operating expenses of the land and building. Lease expense for 2014 and 2013 was $[redacted] and $[redacted], respectively. At December 31, 2014, the lease payments were in the aggregate of $[redacted] per month. Subsequent to the balance sheet date, the remaining term of this lease was assumed by a company that purchased the assets of FiberCloud (see Note 11).

FiberCloud assumed a lease agreement for leased office space in Bellingham, Washington. The term of the agreement was for ten years with a five-year renewal option. As defined in the agreement, base rent can be increased by the scheduled amounts as noted in the agreement and FiberCloud's prorata share of reasonable and customary operating expenses of the land and building. Lease expense for 2014 and 2013 was $[redacted] and $[redacted], respectively. At December 31, 2014, the lease payment was $[redacted] per month. The initial term of the lease expired in October 2009, and was renewed until October 31, 2014 and includes a five-year renewal option which was exercised by the Company. Subsequent to the balance sheet date the remaining term of this lease was assumed by a company that purchased the assets of FiberCloud (see Note 11).

FiberCloud assumed three lease agreements during 2004 and one lease agreement during 2005 for office space in Seattle, Washington. The terms of the agreements range from five to seven years. As defined in the agreements, base rents can be increased by the scheduled amounts as noted in the agreements and FiberCloud's prorata share of reasonable and customary operating expenses of the land and building. Total lease expense for 2014 and 2013 was $[redacted] and $[redacted], respectively. At December 31, 2014, the lease payments were in the aggregate $[redacted] per month. The terms of the agreements in effect at December 31, 2014 expire April 30, 2017. Subsequent to the balance sheet date the remaining term of two of the lease agreements was assumed by a company that purchased the assets of FiberCloud (see Note 11). The third lease was subleased to the purchaser effective April 4, 2015 on a month-to-month basis with monthly rent of $[redacted].

The Company and Subsidiaries have various agreements under which telecommunications bandwidth and transport services are obtained from several service providers. The various service agreements include various termination dates through February 2019. Expense under these agreements for 2014 and 2013 was $[redacted] and $[redacted], respectively.

NOTE 8 - LEASES AND SERVICE AGREEMENTS (Continued)

Future minimum payments for the next five years under the terms of the agreements referred to above in this Note 8, as determined by the current monthly or scheduled payments, are as follows:

2014	[redacted]
2015	
2016	
2017	
2018	

NOTE 9 - PENSION PLAN AND 401(k) PLAN

The Company provides a 401(k) plan. Eligibility for participation in the 401(k) plan begins on the first day of the first month following one year of service and attainment of age 21. The 401(k) plan provides for the Company to make matching contributions. The safe harbor matching contribution rate is equal to [redacted]% of the first [redacted]% of the participant's 401(k) elective deferral contributions, plus [redacted]% of the participants 401(k) elective deferral contributions between [redacted]% and [redacted]%. At the discretion of the Company, the 401(k) plan also provides for an additional match up to [redacted]% of qualifying payroll and a non-elective contribution amount. Company contributions were made to qualifying employees' self-directed 401(k) plan investment accounts described above in the amounts of $[redacted] for 2014 and $[redacted] for 2013. During 2014 and 2013, the Company elected to not make any additional matching or non-elective contributions to employee accounts.

The Company's wholly-owned subsidiaries except WiFire, Inc. are adopting employers of the Company's 401(k) plan.

NOTE 10 - OTHER RELATED PARTY TRANSACTIONS

Other accounts receivable includes amounts receivable from Hat Island Telephone Company ("Hat") and the Company's former sole stockholder of record. Hat is 100% owned by the Company's former sole stockholder of record. The amounts receivable from Hat are generally the result of work performed by Company work crews on behalf of Hat and Hat's former sole stockholder of record. The amounts are unsecured, non-interest-bearing and are to be repaid in the ordinary course of business.

In addition, the Company rents real property from the Company's former sole stockholder of record. The amount of rent for 2014 and 2013 was $[redacted] and $[redacted], respectively.

NOTE 11 - SUBSEQUENT EVENTS

On March 31, 2015 the Company sold FiberCloud's equipment, customer contracts, customer lists, marketing information and trademarks and trade names to an unrelated company that operates in the same industry as FiberCloud. The purchase price is $[redacted], with possible adjustments for differences between closing date working capital and target date working capital as set forth in the asset purchase agreement. The purchaser also obtained an assignment of FiberCloud's interests in operating leases for data center space, transport, bandwidth and dark fiber leases. The assets sold had a carrying value of $[redacted] with accumulated depreciation of $[redacted] with a net book value of $[redacted] at March 31, 2015 resulting in a loss of approximately $[redacted] for financial statement purposes with the final amounts depending on final allocation of purchase price with possible adjustments as noted above. The leases assumed by the purchaser had future minimum lease payments totaling approximately $[redacted] over the next three years.

For the years ending December 31, 2014 and 2013 FiberCloud had revenues of $[redacted] and $[redacted] and expenses of $[redacted] and $[redacted] resulting in net losses of $[redacted] and $[redacted], respectively.