

**ICTC Group, Inc. and Subsidiaries**

**Financial Report to Shareholders**

**March 31, 2017**

**ICTC Group, Inc. and Subsidiaries**  
**Condensed Consolidated Financial Statements**  
**March 31, 2017**

**Part I - Financial Information**

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**Part 1 - Financial Information**  
**Item 1. Financial Statements**

**ICTC Group, Inc. and Subsidiaries**  
**Condensed Consolidated Balance Sheets**

	March 31, 2017 <u>(Unaudited)</u>	December 31, 2016 *
<b>Assets</b>		
Current Assets		
Cash and cash equivalents	\$ 3,428,918	\$ 3,071,376
Accounts receivable, net of allowances of \$4,000	498,270	443,664
Materials and supplies	322,835	225,011
Deferred income taxes	75,453	75,453
Prepayments	<u>183,688</u>	<u>221,551</u>
Total current assets	<u>4,509,164</u>	<u>4,037,055</u>
Noncurrent Assets		
Marketable Securities	794,162	651,138
Other investments	245,971	252,840
Equity method investments	2,141,560	2,040,702
Goodwill	<u>1,772,179</u>	<u>1,772,179</u>
Total noncurrent assets	<u>4,953,871</u>	<u>4,716,859</u>
Telecommunications Plant and Equipment		
In service	22,413,174	22,491,224
Under construction	<u>47,892</u>	<u>16,913</u>
	22,461,066	22,508,137
Less accumulated depreciation and amortization	<u>16,036,347</u>	<u>15,895,330</u>
Net telecommunications plant and equipment	<u>6,424,718</u>	<u>6,612,807</u>
Total Assets	<u>\$ 15,887,753</u>	<u>\$ 15,366,721</u>

\*Derived from audited financial statements

ICTC Group, Inc. and Subsidiaries  
Condensed Consolidated Balance Sheets

	March 31, 2017 <u>(Unaudited)</u>	December 31, 2016 *
<b>Liabilities and Stockholders' Equity</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 61,392	\$ 70,319
Current maturities of long-term debt	27,200	27,200
Accrued income taxes	185,728	6,155
Other current liabilities	<u>335,604</u>	<u>297,722</u>
Total current liabilities	<u>609,924</u>	<u>401,396</u>
<b>Long-Term Debt</b>		
Broadband Initiatives Program Loan	611,541	618,436
Other long-term debt	<u>2,071,800</u>	<u>2,071,800</u>
Total Long-Term Debt	<u>2,683,341</u>	<u>2,690,236</u>
<b>Other Liabilities</b>		
Deferred income taxes	<u>2,552,057</u>	<u>2,558,319</u>
Total other liabilities	<u>2,552,057</u>	<u>2,558,319</u>
Total liabilities	<u>5,845,322</u>	<u>5,649,951</u>
<b>Stockholders' equity</b>		
Preferred Stock: \$.0001 par value; 1,000,000 shares authorized		
No shares outstanding	-	-
Common Stock: \$.0001 par value; 2,000,000 shares authorized		
Issued and outstanding: 380,884 and 381,734	41	41
Treasury Stock; 27,292 and 25,692 shares	(596,190)	(532,348)
Additional paid in capital	1,851,241	1,827,241
Comprehensive Income	76,890	87,542
Retained earnings	<u>8,710,449</u>	<u>8,334,294</u>
Total stockholders' equity	<u>10,042,431</u>	<u>9,716,770</u>
Total Liabilities and Stockholders' Equity	<u>\$ 15,887,753</u>	<u>\$ 15,366,721</u>

\*Derived from audited financial statements

ICTC Group, Inc. and Subsidiaries  
Condensed Consolidated Statements of Income

	<u>Three Months Ended Mar 31</u>	
	2017	2016
	<u>(Unaudited)</u>	<u>(Unaudited)</u>
<b>Revenues</b>		
Local telephone service revenue	\$ 113,942	\$ 113,305
Universal service and access revenue	959,192	615,597
Internet revenue	161,989	107,372
Facility lease revenue	121,239	123,347
Miscellaneous revenue	<u>8,961</u>	<u>13,691</u>
Total operating revenues	<u>1,365,323</u>	<u>973,313</u>
<b>Costs and expenses</b>		
Plant operations, excluding depreciation	441,807	382,724
Depreciation	251,460	226,996
Customer operations	41,881	37,417
Corporate operations	269,068	257,588
Operating taxes, other	<u>5,897</u>	<u>3,259</u>
Total operating expenses	<u>1,010,113</u>	<u>907,983</u>
Operating Income	<u>355,210</u>	<u>65,330</u>
<b>Nonoperating Income (Expense)</b>		
Dividend income	100,868	140,390
Other income	21,124	-
Equity in earnings of investee	<u>100,858</u>	<u>104,414</u>
Total nonoperating income	<u>222,850</u>	<u>244,804</u>
Income Before Interest and Income Taxes	578,060	310,135
Interest Expense	<u>22,332</u>	<u>22,545</u>
Income Before Income Taxes	555,728	287,590
Income Tax Expense	<u>179,573</u>	<u>70,244</u>
Net Income	<u>\$ 376,155</u>	<u>\$ 217,346</u>
Basic and Diluted Weighted Average Common Shares Outstanding	380,976	382,757
Basic and Diluted Earnings Per Share	\$ 0.99	\$ 0.57

ICTC Group, Inc. and Subsidiaries  
Condensed Consolidated Statements of Stockholders' Equity

	Preferred Stock	Common Stock	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Additional paid in Capital	Retained Earnings	Total
Balance, January 1, 2017	\$ -	\$ 41	\$(532,348)	\$ 87,542	\$ 1,827,241	\$8,334,294	\$ 9,716,770
Purchase of Treasury Shares			(63,842)				(63,842)
Comprehensive Loss				(10,652)			(10,652)
Issued Stock					24,000		24,000
Net income						376,155	376,155
Balance, March 31, 2017	<u>\$ -</u>	<u>\$ 41</u>	<u>\$(596,190)</u>	<u>\$ 76,890</u>	<u>\$ 1,851,241</u>	<u>\$8,710,449</u>	<u>\$ 10,042,431</u>

ICTC Group, Inc. and Subsidiaries  
Condensed Consolidated Statements of Cash Flows

	<u>Three Months Ended March 31</u>	
	2017	2016
	(Unaudited)	(Unaudited)
<b>Operating Activities</b>		
Net income	\$ 376,155	\$ 217,346
Adjustments to reconcile net income to net cash from operating activities		
Depreciation	251,460	226,996
Earnings from equity investments	(100,858)	(104,414)
Distributions received - equity investments	-	-
Deferred income taxes	-	-
Distributions/(Earnings) from other investments	6,869	1,320
Change in current assets and current liabilities		
Accounts receivable	(54,606)	98,589
Prepaid income taxes	-	-
Prepayments	37,863	38,995
Accounts payable	(8,927)	(27,925)
Accrued income taxes	179,573	64,944
Other current liabilities	37,882	20,020
<b>Net Cash from Operating Activities</b>	<b>725,411</b>	<b>535,870</b>
<b>Investing Activities</b>		
Purchase of plant and equipment	(63,372)	(171,001)
Decrease (Increase) in materials and supplies	(97,824)	(22,234)
Purchase of Marketable Securities	(159,937)	(116,978)
<b>Net Cash (used for) Investing Activities</b>	<b>(321,133)</b>	<b>(310,213)</b>
<b>Financing Activities</b>		
Repurchase of Common Stock - 1600 and 391 shares	(63,842)	(8,638)
Additional paid in capital	24,000	-
Principal payments on long-term debt	(6,895)	(6,829)
<b>Net Cash from (used for) Financing Activities</b>	<b>(46,737)</b>	<b>(15,467)</b>
<b>Net Change in Cash and Cash Equivalents</b>	357,542	210,189
Cash and Cash Equivalents, Beginning of Period	3,071,376	3,016,485
Cash and Cash Equivalents, End of Period	<b>\$ 3,428,918</b>	<b>\$ 3,226,674</b>
<b>Supplementary Disclosures of Cash Flow Information</b>		
Cash payments for interest	\$ 22,332	\$ 22,545
Cash payments for income taxes, net of refunds	\$ -	\$ 5,300
<b>Non-cash investing and financing activities</b>		
Accounts payable - purchase of property and equipment		
Beginning of Period	\$ -	\$ 7,919
End of Period	\$ 32,729	\$ 13,425



## **Note 1 - Nature of Operations and Summary of Significant Accounting Policies**

### **Organization**

ICTC Group, Inc. (the “Company”) serves as a holding company for Lynch Telephone II, LLC (“Lynch II”), which in turn serves as a holding company for Inter-Community Telephone Company, LLC (“Inter-Community”) and Valley Communications, Inc. (“Valley”)(collectively, the “Subsidiaries”). Inter-Community is a rural local exchange company (“RLEC”) serving communities in southeastern North Dakota providing regulated telephone service; Valley provides internet and other non-regulated services. The Company operates in one business segment, telecommunications.

### **Basis of Presentation and Consolidation**

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information. Accordingly, they are not audited and do not include all of the information and footnotes required for complete financial statements. The consolidated financial statements and footnotes should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s annual report for the year ended December 31, 2016. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three month period ended March 31, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017. The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

The consolidated financial statements include the accounts of Lynch II, Inter-Community and Valley. All assets and liabilities of the Subsidiaries are consolidated with the assets and liabilities of the Company. All significant inter-company accounts have been eliminated.

### **Regulatory Accounting**

The Company’s public utility activities are regulated by the Federal Communications Commission (FCC). The North Dakota Public Service Commission does not regulate RLEC’s with fewer than 8,000 access lines, such as Inter-Community. The Company follows the FCC’s Uniform System of Accounts, Part 32 of the FCC Rules and Regulations.

Where applicable, this regulated accounting recognizes the economic effects of rate regulation by recording costs and a return on investment; as such, amounts are recovered through rates authorized by regulatory authorities. Factors that could give rise to the discontinuance of regulatory accounting practices include (1) increasing competition restricting the Company’s wireline business’ ability to establish prices to recover specific costs and (2) significant changes in the manner in which rates are set by regulators from cost based regulation to another form of regulation. The Company periodically reviews the applicability of regulatory accounting guidelines based on the developments in its current regulatory and competitive environments.

### **Accounting Estimates**

The preparation of consolidated 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 amounts of assets and liabilities at the date of the consolidated financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### **Concentrations of Business and Credit Risk**

The Company provides telephone, internet and other nonregulated services on account to its customers located in southeastern North Dakota. The Company also provides access service on account to various long distance companies, which provide toll service to the Company's customers.

The FCC has proposed significant changes to the rules affecting the revenues of RLECs. The Company serves high cost rural areas and receives a significant portion of its revenues from federal support mechanisms and access revenues from long distance carriers. The Company's revenues are significantly dependent on the continuation and level of such support mechanisms.

The Company's cash balances are maintained in bank depositories and periodically exceed federally insured limits.

### **Cash and Cash Equivalents**

For purposes of reporting cash flows, the Company considers all cash deposits with an original maturity of three months or less to be cash and cash equivalents.

### **Accounts Receivable**

Trade receivables are uncollateralized customer obligations due under normal trade terms requiring payment within 30 days from the invoice date. The receivables are non-interest bearing. Payments on trade receivables are applied to the applicable unpaid invoices. The carrying amount of the trade receivables is reduced by an amount that reflects management's best estimate of the amounts that will not be collected.

### **Materials and Supplies**

Inventories are stated at the lower of average cost or market.

### **Investments**

Investments in limited liability companies (LLC's) are accounted for using the equity method. Under the equity method, the investment is initially recorded at cost, then reduced by the dividends and increased or decreased by the investor's proportionate share of the investee's net earnings or loss. All other investments are stated at cost.

## **Goodwill**

Goodwill is tested annually for impairment, or more frequently, if deemed necessary. The Company tests goodwill for impairment using a two-step process. The first step is a screen for potential impairment in which the Company determines its fair value based on a number of subjective factors, including: (a) appropriate weighting of valuation approaches (income approach, market approach and comparable company approach), (b) estimates of our future cost structure, (c) discount rates for estimated cash flows, (d) selection of peer group companies for our market approach, (e) required level of working capital, (f) assumed terminal value, and (g) time horizon of cash flow forecasts. The Company estimates the fair value using Level 3 inputs as defined in the fair value hierarchy.

If such tests indicate potential impairment due to the carrying value of the reporting unit exceeding its fair value, then a second step measures the amount of impairment, if any. The Company performed the required annual tests as of December 31, 2016, and determined that there was no impairment at that time. There were no impairment losses recorded during the periods ending March 31, 2017 and 2016.

## **Telecommunications Plant and Equipment**

Additions to plant and equipment are recorded at cost, which includes contracted work, direct labor and materials, and allocable overheads. When units of plant and equipment are retired, sold, or otherwise disposed of in the ordinary course of business, their average book cost less net salvage is charged to accumulated depreciation. Maintenance and repair costs and the replacement and renewal of items determined to be less than units of plant and equipment are charged to expense.

## **Depreciation**

The majority of the Company's plant and equipment is plant used for the wireline telephone business. Depreciation is based on the composite group remaining life method and straight-line composite rates. This methodology provides for the recognition of the cost of the remaining investment in telephone plant and equipment less anticipated positive net salvage value, over the remaining asset lives. When depreciable telephone plant is replaced or retired, the carrying amount of such plant is deducted from the respective accounts and charged to accumulated depreciation and no gain or loss is recognized. Use of this methodology requires the periodic revision of depreciation rates. In the evaluation of asset lives, multiple factors are considered, including expected future retirements, technology changes and the adequacy of depreciation reserves.

## **Impairment of Long-Lived Assets**

Long-lived assets, such as telecommunications plant, and purchased intangibles subject to amortization, are reviewed from 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 group to estimated undiscounted future cash flows expected to be generated by the asset group. If the carrying amount of an asset group exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset group exceeds the fair value of the asset group. There were no asset impairments recorded during the periods ended March 31, 2017 and 2016.

## **Income Taxes**

The Company will file federal and state income tax returns on a consolidated basis. All income taxes reflected by the Company have been computed on a separate return basis. The Company follows the liability method of accounting for income taxes, under which deferred income tax assets and liabilities are determined based on the difference between financial reporting and income tax bases of assets and liabilities using the enacted marginal tax rates and laws expected to be in effect when the differences are expected to reverse. Temporary differences result primarily from depreciation and certain accruals.

The Company has evaluated whether it was necessary to recognize any benefit from uncertain tax positions in currently open tax periods and determined that there are no material uncertainties within its filed tax returns. As of March 31, 2017 and March 31, 2016, the unrecognized tax benefit accrual was zero. The Company would recognize future accrued interest and penalties related to unrecognized tax benefits in income tax, if incurred. Generally, the Company is no longer subject to Federal and state tax examinations by tax authorities for years prior to 2010.

## **Government Grants**

The Company has received grant money from the Broadband Initiatives Program administered by RUS (Note 5). Government grants are accrued as a receivable when we determine we have complied with the conditions attached to the grant arrangement. Government grants received in advance are recorded as Deferred Broadband Initiatives Program grant funds on the Balance Sheet. Grants received for reimbursement of capital expenditures is accounted for as a deduction from the cost of the asset. Depreciation is calculated and recorded based on our net investment. The impact of the grant is reflected in earnings as a reduction in depreciation. Grant funds received are shown as inflows in the investing activities section of the Consolidated Statements of Cash Flows.

## **Revenue Recognition**

Telephone service revenue is primarily derived from regulated local, intrastate and interstate access services and recognized as services are provided.

Local access revenues come from providing local telephone exchange services and are billed to local end-users in advance in accordance with tariffs approved by the state regulatory commission. Such advance billings are initially deferred and recognized as revenue when earned.

Revenue that is billed in arrears includes nonrecurring intrastate and interstate network access services, nonrecurring local services and long distance services. The earned but unbilled portion of this revenue is recognized as revenue in the period that the services are provided.

Revenue from intrastate access is based on tariffs approved by the state regulatory commission. Revenue from interstate access is derived from settlements with NECA. NECA was created by the FCC to administer access rates and revenue pooling on behalf of local exchange carriers who elected to participate in a pooling arrangement. Interstate settlements, including amounts received under Universal Service Fund mechanisms, are determined based on the Company's cost of providing telecommunications service, including investments in specific types of infrastructure and operating expenses and taxes.

Interstate access revenue recognition is based on management's estimate of the final earning settlement of the NECA pools. For the NECA Common Line pool, the 2017 and 2016 rates-of-return are expected to equal the authorized rate-of-return of 10.75%; therefore, interstate revenues were increased to reflect the additional revenues which are expected to be received from NECA once the Common Line pool settlements are finalized.

The Company also leases use of telecommunications facilities on a short term basis to other telecommunications companies. Revenue from the leases is recognized monthly when earned.

Other ancillary revenues, derived from the provision of directory advertising and billing and collection services, are recognized as services are provided based on the rates under the respective contract. Non-regulated operations are included in other income in the accompanying consolidated statements of income.

### **Advertising Costs**

Advertising costs are expensed as incurred.

### **Sales Taxes**

The Company has customers in North Dakota and its municipalities in which those governmental units impose a sales tax on certain sales. The Company collects those sales taxes from its customers and remits the entire amount to the various governmental units. The Company's accounting policy is to exclude the tax collected and remitted from revenue and cost of revenue.

### **Fair Value of Financial Instruments**

The carrying value of the Company's financial instruments, including cash and cash equivalents, accounts receivable, accounts payable, and long-term notes payable approximate their fair value as of March 31, 2017 and March 31, 2016.

The cost investments are carried at historical cost due to no readily determinable fair value for those instruments being available. Management believes there has been no other than temporary impairment in the investments.

### **Earnings per Common Share**

The Company computes net income per common share in accordance with the provision included in ASC 260, *Earnings per Share* ("ASC 260"). Under ASC 260, basic and diluted income per share is computed by dividing net income available to stockholders by the weighted average number of common shares and common share equivalents outstanding during the period. Basic income per common share excludes the effect of potentially dilutive securities, while diluted income per common share reflects the potential dilution that would occur if securities or other contracts to issue common shares were exercised for, converted into or otherwise resulted in the issuance of common shares. The company had no potentially dilutive common share equivalents outstanding at March 31, 2017 and March 31, 2016.

**Reclassifications**

Certain reclassifications have been made to the 2013 consolidated financial statement presentation in order to conform to the 2014 consolidated financial statement presentation. The reclassifications had no effect on net income or equity.

**Recent Accounting Pronouncements**

We reviewed all significant newly issued accounting pronouncements and determined they are either not applicable to our business or that no material effect is expected on our financial position and results of operations.

**Note 2 - Telecommunications Plant and Equipment**

Depreciation and amortization expense for the three months ended March 31, 2017 and 2016 was \$251,460 and \$226,996 respectively.

**Note 3 - Equity Method Investments**

	March 31, 2017 <u>(Unaudited)</u>	<u>December 31, 2016</u>
Dakota Carrier Network, LLC (3.433% ownership at equity)	<u>\$2,141,560</u>	<u>\$2,040,702</u>

The Company recognized equity earnings from Dakota Carrier Network, LLC of \$100,858 and \$104,414 during the three months ended March 31, 2017 and 2016 respectively. The Company received no distributions during the three months ended March 31, 2017 and 2016, respectively.

ICTC Group, Inc. and Subsidiaries  
Notes to Condensed Consolidated Financial Statements  
December 31, 2016

Condensed financial information of Dakota Carrier Network, LLC is as follows:

	<u>March 31,</u> <u>2017</u>	<u>December 31,</u> <u>2016</u>
<b>Assets</b>		
Current assets	\$ 7,443,940	\$ 4,864,734
Other assets	2,647,372	2,748,288
Property, net	<u>53,280,278</u>	<u>53,556,915</u>
Total Assets	<u>\$ 63,371,590</u>	<u>\$ 61,169,937</u>
<b>Liabilities and Members' Equity</b>		
Current liabilities	\$ 387,418	\$ 1,210,211
Other Liabilities	\$ 599,612	\$ 513,205
Members' equity	<u>62,384,560</u>	<u>59,446,521</u>
Total Liabilities and Members' Equity	<u>\$ 63,371,590</u>	<u>\$ 61,169,937</u>
	<u>Three months ended March 31,</u>	
	<u>2017</u>	<u>2016</u>
	<u>(Unaudited)</u>	<u>(Unaudited)</u>
<b>Operations</b>		
Revenues	\$ 11,915,464	\$ 11,689,411
Expenses	<u>8,977,426</u>	<u>8,646,993</u>
Net income	<u>\$ 2,938,038</u>	<u>\$ 3,042,418</u>

**Note 4 - Long-Term Debt**

The Company has subordinated notes with former shareholders for \$2,071,800 as of March 31, 2017 and March 31, 2016. The interest rates on the notes range from 2% to 6% and the maturity date is December 31, 2022. Interest on the notes is paid quarterly. The notes may be prepaid at any time without penalty.

The Company received a loan of \$713,289 from the Broadband Initiatives Program which has a balance of \$638,741 as of March 31, 2017. See Note 5 for additional information relating to the loan/grant agreement. The loan is due in monthly payments of principal and interest over 21 years at an average interest rate of 3.02%. The loan/grant agreement includes certain financial and other covenant requirements.

It is estimated that principal repayments on the Company's debt for the next five years will be as follows:

Years Ended December 31,

2017	27,000
2018	27,000
2019	28,000
2020	29,000
2021	30,000

**Note 5 - Broadband Initiatives Program**

The Company was awarded a stimulus loan and grant pursuant to the American Recovery and Reinvestment Act of 2009 to finance the construction of a broadband infrastructure project in rural areas. The \$2,338,651 project was completed during 2014. The project is being funded through a broadband loan from the Rural Utilities Service (RUS) of \$713,289, and a grant through the Broadband Initiatives Program administered by RUS, of \$1,625,362. The Company has received the full amount of \$713,289 in advances on the broadband loan and \$1,625,362 in grant funds relating to the project. As of March 31, 2017, the balance on these loans is \$638,741.

**Note 6 - Stockholders' Equity**

CIBL, Inc. ("CIBL"), has voting control of the company through its control of a total of 212,556 shares, including 46,000 shares it does not own but has voting control, of ICTC's class A stock or 55.8% of the 380,884 Class A shares that are currently outstanding.

**Note 7 - Subsequent Events and Other**

The Company has evaluated subsequent events through April 28, 2017.