

Summary of Statements of Net Income—Unaudited

Amounts in millions except per share amounts

| | Quarter Ended September 30 | | | | Nine Months Ended September 30 | | | |
|---|----------------------------|--------|--------|----------|--------------------------------|--------|--------|----------|
| | 2016 | 2015 | Change | % Change | 2016 | 2015 | Change | % Change |
| Net operating revenue (after uncollectibles): | | | | | | | | |
| Internet and communications | \$19.2 | \$18.5 | \$0.7 | 4% | \$57.5 | \$55.0 | \$2.5 | 5% |
| Information technology services and hardware | 10.2 | 8.7 | 1.5 | 17% | 28.4 | 18.1 | 10.3 | 57% |
| Net operating revenue | 29.4 | 27.2 | 2.2 | 8% | 85.9 | 73.1 | 12.8 | 18% |
| Operating expense: | | | | | | | | |
| Cost of sales and service | 14.4 | 12.9 | 1.5 | 12% | 40.9 | 32.0 | 8.9 | 28% |
| Selling, general, and administrative | 8.1 | 7.6 | 0.5 | 7% | 24.0 | 21.9 | 2.1 | 10% |
| Depreciation and amortization | 5.0 | 4.9 | 0.1 | 2% | 14.9 | 14.4 | 0.5 | 4% |
| Total operating expense | 27.5 | 25.4 | 2.1 | 8% | 79.8 | 68.3 | 11.5 | 17% |
| Operating income | 1.9 | 1.8 | 0.1 | 5% | 6.1 | 4.8 | 1.3 | 27% |
| Nonoperating income | 1.8 | 1.4 | 0.4 | 28% | 5.1 | 5.4 | (0.3) | -5% |
| Income before taxes | 3.7 | 3.2 | 0.5 | 15% | 11.2 | 10.2 | 1.0 | 10% |
| Income taxes | 1.4 | 1.2 | 0.2 | 16% | 4.1 | 3.8 | 0.3 | 8% |
| Net income | \$2.3 | \$2.0 | \$0.3 | 15% | \$7.1 | \$6.4 | \$0.7 | 11% |
| Earnings per share | \$1.04 | \$0.89 | \$0.15 | 17% | \$3.13 | \$2.80 | \$0.33 | 12% |

Summary of Net Operating Revenue—Unaudited

| | Quarter Ended September 30 | | | | Nine Months Ended September 30 | | | |
|---|----------------------------|---------------|--------------|----------|--------------------------------|---------------|---------------|----------|
| | 2016 | 2015 | Change | % Change | 2016 | 2015 | Change | % Change |
| TOTAL NET OPERATING REVENUE | | | | | | | | |
| Internet and communications: | | | | | | | | |
| Strategic | \$9.7 | \$8.4 | \$1.3 | 15% | \$28.6 | \$24.9 | \$3.7 | 15% |
| Legacy | 9.5 | 10.1 | (0.6) | -6% | 28.9 | 30.1 | (1.2) | -4% |
| Total internet and communications | 19.2 | 18.5 | 0.7 | 4% | 57.5 | 55.0 | 2.5 | 5% |
| IT services and hardware-strategic | 10.2 | 8.7 | 1.5 | 17% | 28.4 | 18.1 | 10.3 | 57% |
| Total net operating revenue | <u>\$29.4</u> | <u>\$27.2</u> | <u>\$2.2</u> | 8% | <u>\$85.9</u> | <u>\$73.1</u> | <u>\$12.8</u> | 18% |
| TOTAL BUSINESS & WHOLESALE NOR | | | | | | | | |
| Internet and communications: | | | | | | | | |
| Strategic | \$2.6 | \$2.3 | \$0.3 | 13% | \$7.6 | \$7.0 | \$0.6 | 8% |
| Legacy | 6.6 | 6.7 | (0.1) | -1% | 20.1 | 20.2 | (0.1) | -1% |
| Total internet and communications | 9.2 | 9.0 | 0.2 | 2% | 27.7 | 27.2 | 0.5 | 2% |
| IT services and hardware-strategic | 10.2 | 8.7 | 1.5 | 17% | 28.4 | 18.1 | 10.3 | 56% |
| Total net operating revenue | <u>\$19.4</u> | <u>\$17.7</u> | <u>\$1.7</u> | 10% | <u>\$56.1</u> | <u>\$45.3</u> | <u>\$10.8</u> | 24% |
| TOTAL CONSUMER NOR | | | | | | | | |
| Internet and communications: | | | | | | | | |
| Strategic | \$7.2 | \$6.2 | \$1.0 | 16% | \$21.0 | \$17.9 | \$3.1 | 17% |
| Legacy | 2.8 | 3.3 | (0.5) | -15% | 8.8 | 9.9 | (1.1) | -11% |
| Total net operating revenue | <u>\$10.0</u> | <u>\$9.5</u> | <u>\$0.5</u> | 5% | <u>\$29.8</u> | <u>\$27.8</u> | <u>\$2.0</u> | 7% |

Consolidated Balance Sheets—Unaudited

| At September 30, | 2016 | 2015 |
|---|----------------|----------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 10,935,888 | \$ 2,449,452 |
| Accounts receivable, net of allowance for doubtful accounts | 9,304,103 | 12,374,678 |
| Materials and supplies | 2,398,997 | 2,105,708 |
| Prepayments | 1,570,760 | 1,657,129 |
| Income taxes recoverable | 235,759 | 263,883 |
| Deferred income taxes | 683,692 | 738,922 |
| Total current assets | 25,129,199 | 19,589,772 |
| Property, plant, and equipment | 509,182,622 | 494,881,977 |
| Less accumulated depreciation | 359,077,441 | 342,722,706 |
| Property, plant, and equipment, net | 150,105,181 | 152,159,271 |
| Other assets: | | |
| Investment securities | 586,456 | 4,415,855 |
| Investments in unconsolidated entities | 9,930,486 | 9,185,114 |
| Intangibles, net of amortization | 15,551,314 | 15,135,242 |
| Goodwill | 31,794,755 | 33,808,546 |
| Other noncurrent assets | 921,097 | 1,072,539 |
| Total other assets | 58,784,108 | 63,617,296 |
| Total assets | \$ 234,018,488 | \$ 235,366,339 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Revolving credit note | \$ - | \$ 7,500,000 |
| Current maturities of bank note | 625,000 | 5,500,000 |
| Current maturities of capital lease obligations | 154,018 | 142,253 |
| Accounts payable and payroll withholdings | 1,934,553 | 3,272,775 |
| Advance billings and customer deposits | 3,632,672 | 4,204,138 |
| Income taxes payable | - | 1,457 |
| Accrued expenses | 6,253,438 | 6,816,982 |
| Accrued taxes | 1,245,865 | 1,143,308 |
| Total current liabilities | 13,845,546 | 28,580,913 |
| Other liabilities: | | |
| Bank note, net of current maturities | 48,986,361 | 37,125,000 |
| Capital lease obligations, net of current maturities | 5,834,297 | 5,988,315 |
| Deferred income taxes | 26,845,853 | 25,132,412 |
| Accrued pension benefits | 40,912,459 | 31,560,270 |
| Accrued postretirement benefits | 618,412 | 525,124 |
| Other liabilities and deferred credits | 1,366,456 | 1,553,680 |
| Total other liabilities | 124,563,838 | 101,884,801 |
| Total liabilities | 138,409,384 | 130,465,714 |
| Stockholders' equity: | | |
| Preferred stock | 1,874,600 | 1,896,600 |
| Common stock | 11,346,775 | 11,370,200 |
| Paid in capital | 64,588 | 55,298 |
| Retained earnings | 115,334,911 | 116,921,812 |
| Accumulated other comprehensive loss | (33,011,770) | (25,343,285) |
| Total stockholders' equity | 95,609,104 | 104,900,625 |
| Total liabilities and stockholders' equity | \$ 234,018,488 | \$ 235,366,339 |

Consolidated Statements of Net Income—Unaudited

| Nine Months Ended September 30, | 2016 | 2015 |
|--|---------------|---------------|
| Operating revenues: | | |
| Internet and communications: | | |
| Strategic internet and data | \$ 21,065,588 | \$ 18,896,826 |
| Strategic entertainment | 8,095,774 | 6,744,026 |
| Legacy voice | 25,196,772 | 25,785,872 |
| Legacy long distance | 1,998,043 | 2,198,009 |
| Legacy advertising and search | 1,919,545 | 2,079,463 |
| Total internet and communications | 58,275,722 | 55,704,196 |
| Information technology services and hardware: | | |
| Strategic telecom and IT equipment | 11,165,416 | 4,591,390 |
| Strategic colocation | 8,653,218 | 8,658,332 |
| Strategic managed and professional services | 7,146,751 | 3,555,168 |
| Strategic UCAAS | 1,424,533 | 1,337,456 |
| Total IT services and hardware | 28,389,918 | 18,142,346 |
| Total operating revenues | 86,665,640 | 73,846,542 |
| Less uncollectible revenue | 711,976 | 694,330 |
| Net operating revenues | 85,953,664 | 73,152,212 |
| Cost of sales and service: | | |
| General support | 5,277,925 | 4,734,444 |
| Central office | 6,214,494 | 6,466,400 |
| Communication termination | 19,784,851 | 12,027,097 |
| Cable and wire facilities | 2,421,443 | 2,645,596 |
| Network operations | 7,202,427 | 6,168,975 |
| Total cost of sales and service | 40,901,140 | 32,042,512 |
| Gross margin | 45,052,524 | 41,109,700 |
| Depreciation and amortization expense | | |
| | 14,948,331 | 14,369,466 |
| Selling, general, and administrative expense: | | |
| Customer operations | 14,229,248 | 13,382,439 |
| Corporate operations | 8,620,610 | 7,485,798 |
| Taxes, other than income taxes | 1,127,231 | 1,034,114 |
| Total selling, general, and administrative expense | 23,977,089 | 21,902,351 |
| Net operating income | 6,127,104 | 4,837,883 |
| Nonoperating income (expense): | | |
| Interest income | 21,625 | 69,400 |
| Interest expense, net of capitalized interest | (1,173,948) | (855,628) |
| Equity in earnings of unconsolidated entities | 6,260,737 | 6,104,945 |
| Net gain on sale of investment securities | - | 9,545 |
| Other income, net | 42,585 | 71,581 |
| Net nonoperating income | 5,150,999 | 5,399,843 |
| Income before income taxes | 11,278,103 | 10,237,726 |
| Income taxes | | |
| | 4,122,497 | 3,810,395 |
| Net income | 7,155,606 | 6,427,331 |
| Preferred stock dividends | | |
| | 44,742 | 45,317 |
| Net income available to common stockholders | \$ 7,110,864 | \$ 6,382,014 |
| Earnings per average common share | | |
| | \$3.13 | \$2.80 |
| Dividends per common share | | |
| | \$3.90 | \$3.90 |
| Weighted average common shares outstanding | | |
| | 2,272,004 | 2,276,408 |

Consolidated Statements of Comprehensive Income—Unaudited

| Nine Months Ended September 30, | 2016 | 2015 |
|--|--------------|--------------|
| Net income | \$ 7,155,606 | \$ 6,427,331 |
| Other comprehensive income (loss), net of tax: | | |
| Unrealized holding gains (losses) arising during the period, net of tax benefit in 2016 of \$13,608 and tax benefit in 2015 of \$82,853 | (22,594) | (133,930) |
| Other comprehensive income (loss), net of tax | (22,594) | (133,930) |
| Comprehensive income | \$ 7,133,012 | \$ 6,293,401 |

Consolidated Statements of Stockholders' Equity—Unaudited

| Nine Months Ended September 30, | Preferred Stock | Common Stock | Paid in Capital | Retained Earnings | Accumulated Other Comprehensive Income | | | Total Stockholders' Equity |
|---|---------------------|----------------------|--------------------|-----------------------|--|--------------------------|------------------------|----------------------------------|
| | | | | | Retirement Plans | Marketable Securities | Total | |
| Balance, January 1, 2015 | \$ 1,915,200 | \$ 11,395,825 | \$ 53,936 | \$ 119,745,974 | \$ (25,616,655) | \$ 407,300 | \$ (25,209,355) | \$ 107,901,580 |
| Acquisition of stock | (18,600) | (25,625) | 1,362 | | | | | (42,863) |
| Net income | | | | 6,427,331 | | | | 6,427,331 |
| Preferred stock dividends | | | | (45,317) | | | | (45,317) |
| Common stock dividends | | | | (8,879,220) | | | | (8,879,220) |
| Acquisition of common stock in excess of stated value | | | | (326,956) | | | | (326,956) |
| Unrealized gain (loss) on marketable securities, net of tax | | | | | | (133,930) | (133,930) | (133,930) |
| Balance, September 30, 2015 | \$ 1,896,600 | \$ 11,370,200 | \$ 55,298 | \$ 116,921,812 | \$ (25,616,655) | \$ 273,370 | \$ (25,343,285) | \$ 104,900,625 |
| Balance, January 1, 2016 | \$ 1,888,600 | \$ 11,370,200 | \$ 58,658 | \$ 117,296,892 | \$ (33,011,770) | \$ 22,594 | \$ (32,989,176) | \$ 97,625,174 |
| Acquisition of stock | (14,000) | (23,425) | 5,930 | | | | | (31,495) |
| Net income | | | | 7,155,606 | | | | 7,155,606 |
| Preferred stock dividends | | | | (44,742) | | | | (44,742) |
| Common stock dividends | | | | (8,860,541) | | | | (8,860,541) |
| Acquisition of common stock in excess of stated value | | | | (212,304) | | | | (212,304) |
| Unrealized gain (loss) on marketable securities, net of tax | | | | | | (22,594) | (22,594) | (22,594) |
| Balance, September 30, 2016 | \$ 1,874,600 | \$ 11,346,775 | \$ 64,588 | \$ 115,334,911 | \$ (33,011,770) | \$ - | \$ (33,011,770) | \$ 95,609,104 |

Consolidated Statements of Cash Flows—Unaudited

| Nine Months Ended September 30, | 2016 | 2015 |
|---|----------------|--------------|
| Cash flows from operating activities: | | |
| Net income | \$ 7,155,606 | \$ 6,427,331 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 14,948,331 | 14,369,466 |
| Change in the allowance for doubtful accounts | 125,000 | - |
| Loss (gain) on sale of investment securities | - | (9,545) |
| Loss (gain) on sale, disposal, and abandonment of other assets | 61,291 | 180,570 |
| Equity in earnings of unconsolidated entities | (6,260,737) | (6,104,945) |
| Deferred income taxes | 2,343,077 | (1,390,435) |
| Deferred pension and postretirement benefits | 1,846,834 | 1,041,248 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 1,743,475 | 572,919 |
| Materials and supplies | (564,472) | (440,191) |
| Other assets | 5,525,927 | 4,715,982 |
| Accounts payable and payroll withholdings | (3,135,984) | (3,837,774) |
| Accrued expenses | 687,081 | 683,746 |
| Other liabilities | (3,180,167) | (2,097,619) |
| Net cash provided by operating activities | 21,295,262 | 14,110,753 |
| Cash flow from investing activities: | | |
| Additions to property, plant, and equipment | (12,241,701) | (17,297,407) |
| Cost of removal of telephone plant, net of salvage | 5,907 | (25,339) |
| Proceeds from sale of wireless assets-escrow, net | - | 2,350,000 |
| Proceeds from sale of investment securities | - | 3,685,000 |
| Purchases of investment securities | (1,000) | - |
| Investment in the assets of Stalwart Systems, LLC, net of assumed liabilities | - | (9,545,426) |
| Distributions from equity investments | 70,020 | 23,834 |
| Distributions from unconsolidated entities | 4,997,030 | 5,287,555 |
| Net cash provided by (used in) investing activities | (7,169,744) | (15,521,783) |
| Cash flows from financing activities: | | |
| Proceeds from term loan | 50,000,000 | - |
| Principal payments on term loan | (41,250,000) | (4,125,000) |
| Repayments of line of credit, net of proceeds | (4,500,000) | 7,500,000 |
| Principal payments on capital leases | (107,298) | (82,949) |
| Loan origination fees | (405,536) | (6,272) |
| Acquisition of preferred stock | (8,070) | (17,238) |
| Acquisition of common stock | (235,729) | (352,581) |
| Cash dividends paid | (8,905,283) | (8,924,537) |
| Net cash used in financing activities | (5,411,916) | (6,008,577) |
| Net change in cash and cash equivalents | 8,713,602 | (7,419,607) |
| Cash and cash equivalents at beginning of period | 2,222,286 | 9,869,059 |
| Cash and cash equivalents at end of period | \$ 10,935,888 | \$ 2,449,452 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid for (refunds of) income taxes | \$ (2,355,000) | \$ 2,610,000 |
| Cash paid for interest | \$ 1,047,067 | \$ 846,471 |
| Supplemental schedule of noncash investing and financing activities: | | |
| Property, plant, and equipment funded by capital lease obligations | \$ - | \$ 6,213,517 |

I, Jonathan M. Cage, hereby certify that the accompanying unaudited consolidated balance sheets of North State Telecommunications Corporation and Subsidiaries as of September 30, 2016 and 2015 and the related unaudited consolidated statements of net income, comprehensive income, stockholders' equity, and cash flows for the nine months then ended have been prepared from the Corporation's and Subsidiaries' accounting records. Internal accounting controls and review procedures provide assurance that these statements are materially accurate.

This the 24th day of October 2016.



Jonathan M. Cage
VP-Chief Financial Officer