
LICT CORPORATION

Quarterly Report for period ended September 30, 2011

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LICT CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share amounts)

	September 30, 2010	December 31, 2010	September 30, 2011
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 18,037	\$ 15,223	\$ 11,506
Receivables, less allowances of \$881, \$789 and \$884, respectively	7,768	7,348	7,645
Material and supplies	3,230	2,822	3,504
Income tax receivable	--	614	--
Prepaid expenses and other current assets	1,969	1,782	2,875
Total current assets	<u>31,004</u>	<u>27,789</u>	<u>25,530</u>
Property, plant and equipment:			
Land	1,114	1,114	1,114
Buildings and improvements	18,584	18,711	18,931
Machinery and equipment	277,908	280,739	288,016
	<u>297,606</u>	<u>300,564</u>	<u>308,061</u>
Accumulated depreciation	(201,669)	(203,015)	(211,598)
	<u>95,937</u>	<u>97,549</u>	<u>96,463</u>
Goodwill	60,540	60,540	62,540
Other intangibles	3,974	3,895	3,703
Investments in and advances to affiliated companies	5,193	5,270	5,461
Other assets	10,048	10,098	8,571
Total assets	<u>\$ 206,696</u>	<u>\$ 205,141</u>	<u>\$ 202,268</u>

See accompanying Notes to Condensed Consolidated Financial Statements.

LICT CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(in thousands, except share amounts)

	September 30, 2010	December 31, 2010	September 30, 2011
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current liabilities:			
Notes payable to banks	\$ 13,260	\$ 15,660	\$ 14,535
Trade accounts payable	3,741	3,170	2,861
Accrued interest payable	445	382	286
Accrued liabilities	9,223	7,112	7,773
Current maturities of long-term debt	20,381	11,810	9,703
Total current liabilities	47,050	38,134	35,158
Long-term debt	80,724	84,379	77,514
Deferred income taxes	8,958	11,333	14,110
Liability for unrecognized tax benefits	3,391	580	595
Other liabilities	5,468	5,804	4,871
Total liabilities	145,591	140,230	132,248
Commitments and contingencies			
Shareholders' equity			
Common stock, \$0.0001 par value-10,000,000 shares authorized; 26,637.50, issued; 23,989.37, 23,979.37 and 23,573.37 outstanding	--	--	--
Additional paid-in capital	16,586	16,637	16,637
Retained earnings	52,090	55,877	61,859
Accumulated other comprehensive income	43	41	25
Treasury stock, 2,648.13, 2,658.13 and 3,064.13 shares, at cost	(7,928)	(7,953)	(8,868)
Shareholders' equity attributable to LICT	60,791	64,602	69,653
Noncontrolling interests	314	309	367
Total shareholders' equity	61,105	64,911	70,020
Total liabilities and shareholders' equity	\$ 206,696	\$ 205,141	\$ 202,268

See accompanying Notes to Condensed Consolidated Financial Statements.

LICT CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(in thousands, except per share data)

	Three Months Ended September 30,		Nine Months Ended September 30	
	2010	2011	2010	2011
Revenues	\$ 22,714	\$ 23,280	\$ 69,265	\$ 68,149
Costs and expenses:				
Cost of revenue, excluding depreciation	9,803	10,350	28,759	29,973
General and administrative costs at operations	3,517	3,728	10,602	10,689
Corporate office expenses	963	843	2,712	2,409
Depreciation and amortization	4,280	4,410	12,913	12,804
Total Expense	18,563	19,331	54,986	55,875
Operating profit	4,151	3,949	14,279	12,274
Other income (expense):				
Investment income	35	27	1,016	756
Interest expense	(1,787)	(1,551)	(5,364)	(4,891)
Equity in earnings of affiliated companies	774	1,028	1,386	2,145
Gain on sale of investments	216	--	216	--
	(762)	(496)	(2,746)	(1,990)
Income before income taxes	3,389	3,453	11,533	10,284
Provision for income taxes	(1,339)	(1,345)	(4,606)	(4,244)
Net income from continuing operations	2,050	2,108	6,927	6,040
Net income (loss) from discontinued operations	(17)	-	207	-
Noncontrolling interests	(33)	(19)	(72)	(58)
Net income attributable to LICT	\$ 2,000	\$ 2,089	\$ 7,062	\$ 5,982
Basic and diluted weighted average shares	24,244.33	23,656.52	24,274.88	23,859.42
Basic and diluted earnings per share:				
Net income from continuing operations	\$ 84.56	\$ 89.11	\$ 285.36	\$ 253.15
Net income attributable to LICT	82.49	88.31	290.92	250.72

See accompanying Notes to Condensed Consolidated Financial Statements.

LICT CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(Unaudited)
(in thousands, except share data)

	Shares of Common Stock Out- standing	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock	Non- controlling Interest	Total
Balance at December 31, 2010	23,979.37	\$ 0	\$ 16,637	\$ 55,877	\$ 41	\$ (7,953)	\$ 309	\$ 64,911
Net income for the period	--	--	--	5,982	--	--	58	6,040
Unrealized loss on available for sale securities, net	--	--	--	--	(16)	--	--	(16)
Comprehensive income								6,024
Purchase of Treasury Stock	(406.00)					(915)		(915)
Balance at September 30, 2011	23,573.37	\$ 0	\$ 16,637	\$ 61,859	\$ 25	\$ (8,868)	\$ 367	\$ 70,020

See accompanying Notes to Condensed Consolidated Financial Statements.

LICT CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)
(in thousands)

	Nine Months Ended September 30,	
	2010	2011
Operating activities:		
Net Income attributable to LICT	\$ 7,062	\$ 5,982
Adjustments to reconcile net income to net cash provided by operating activities:		
Net income of discontinued operations	(207)	--
Depreciation and amortization	12,913	12,804
Equity in earnings of affiliated companies	(1,386)	(2,145)
Distributions received from affiliated companies	1,050	2,064
Deferred income tax provision (benefit)	310	2,789
Noncontrolling interest	72	58
Changes in operating assets and liabilities:		
Accounts receivables	1,501	(297)
Income tax receivable	1,161	614
Other current assets	(386)	(1,701)
Accounts payable and accrued liabilities	1,071	105
Cash from discontinued operations	630	--
Other	(21)	(1,000)
Net cash provided by operating activities	23,770	19,273
Investing activities:		
Capital expenditures	(10,252)	(11,204)
Acquisition of assets	(2,092)	(400)
Investment in Affiliates	(130)	(109)
Proceeds from cash surrender value of life insurance	--	1,580
Proceeds from sale of investments	420	--
Investing activities of discontinued operations	(288)	--
Other	85	119
Net cash used in investing activities	(12,257)	(10,014)
Financing activities:		
Issuance of long term debt	1,591	--
Repayments of long term debt	(22,259)	(10,936)
Net borrowing (repayment) on lines of credit	6,060	(1,125)
Deferred debt issue cost	(214)	--
Purchase of treasury stock	(725)	(915)
Discontinued operations, cash effect	(500)	--
Net cash used in financing activities	(16,047)	(12,976)
Net increase (decrease) in cash and cash equivalents	(4,534)	(3,717)
Cash and cash equivalents at beginning of period	22,571	15,223
Cash and cash equivalents at end of period	\$ 18,037	\$ 11,506
Cash paid for:		
Interest expense	\$ 5,184	\$ 4,860
Income taxes	1,797	760
Non cash transactions:		
Purchases of property, plant and equipment included in payables or accruals at:		
- End of period	452	774
- Beginning of period	745	549

See accompanying Notes to Condensed Consolidated Financial Statements.

LICT CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

A. Basis of Presentation

LICT Corporation (“LICT” or the “Company”) consolidates the operating results of its subsidiaries. All material intercompany transactions and balances have been eliminated. Investments in affiliates in which the Company does not have a majority voting control, but has the ability to significantly influence management decisions, are accounted for in accordance with the equity method. The Company accounts for the following affiliated companies on the equity basis of accounting: a cellular partnership in California (25% owned) and telecommunications operations in North Dakota (through May 28, 2010), Iowa and New York (5% to 14% owned).

The accompanying unaudited condensed 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. These 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, 2010. 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 and nine month periods ended September 30, 2011 are not necessarily indicative of the results that may be expected for the year ending December 31, 2011. 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.

B. Discontinued Operations -Acquisition and Subsequent Distribution of North Dakota Operations to shareholders

On March 31, 2010, Sunshine PCS Corporation (“Sunshine”) acquired all of the interests of LICT’s subsidiary Lynch Telephone II, LLC, which owns 100% of Inter-Community Telephone Company, LLC (“ICTC”)and Valley Communications, Inc (“Valley”) (Collectively, Sunshine, ICTC and Valley comprise “North Dakota Operations”). Inter-Community is a rural independent local telephone company (“RLEC”) serving communities in southeastern North Dakota providing regulated telephone service and Valley provides internet and other non-regulated services. As consideration, Sunshine issued shares of its Class A common stock reflecting approximately 98% of its outstanding stock, to Lynch Telephone North L.L.C., the parent company of Lynch Telephone II. In order to effectuate the acquisition by Sunshine, LICT utilized \$7.4 million of its line of credit to pay-off the remaining balance of a loan with a bank at Lynch Telephone North that was partially secured by the assets of Lynch Telephone II.

On May 28, 2010, the Company distributed shares of Sunshine (and cash in lieu of fractional shares at the rate of \$50 per share) to its shareholders, spinning off the North Dakota Operations to them. In accordance with accounting rules for presentation of discontinued operations, the results of the North Dakota operations and interest expense on subordinated notes that were assumed by the buyer and bank debt that was required to be repaid as a result of this transaction have been presented as discontinued operations.

Summarized financial information for the North Dakota Operations included in the Consolidated Statements of Operations for the three and nine months ended September 30, 2010 is as follows:

	Three Months Ended September 30, 2010	Nine Months Ended September 30, 2010
	<i>(in thousands)</i>	
Revenue	\$ --	\$ 1,703
Operating income	--	391
Interest expense	(27)	(200)
Equity in earnings of affiliated companies	--	101
Net income (loss)	(17)	207

C. Investments in Affiliated Companies

A subsidiary of LICT owns a 25% partnership interest in a cellular telephone provider in northern California, California RSA #2. As of September 30, 2011, December 31, 2010 and September 30, 2010, the net investment in the partnership was \$4.0 million, \$4.0 million and \$4.0 million, respectively. The Company's share of income from such investment, included in Equity in Earnings of Affiliated Companies was \$2.0 million and \$1.2 million for the nine months ended September 30, 2011 and 2010, respectively.

D. Acquisitions

On May 20, 2010, the Company purchased a cable communications company providing cable television, broadband and voice telephone services to approximately 1,800 customers in rural communities throughout southeastern Kansas for \$2.1 million. The operations will complement an existing CLEC business as well as one of our RLEC operation in southeastern Kansas. Giant Cable had previously been owned by a subsidiary of LICT, and was spun off from LICT as part of the CIBL spin-off in November 2007.

In 2011, the Company's Utah subsidiary purchased cable assets and subscribers from a competitor for \$0.4 million, consisting of 260 video and 80 cable modem subscribers. The acquisition of these assets did not constitute a business, and therefore was accounted for as a purchase of assets. The Company is in the process of valuing the assets acquired.

On June 30, 2010, the Company's California subsidiary purchased subscribers from a competitor for \$0.1 million. The purchase price is included in other intangible assets in the balance sheet.

E. Indebtedness

LICT maintains a short-term line of credit facility totaling \$17.5 million. Borrowings under this and earlier facilities were \$14.5 million, \$15.7 million and \$13.3 million at September 30, 2011, December 31, 2010 and September 30, 2010, respectively. Borrowing under the line of credit facility are included in Notes payable to banks. Long-term debt consists of (all interest rates are at June 30, 2011) (in thousands):

	September 30, 2010	December 31, 2010	September 30, 2011
Rural Electrification Administration (“REA”) and Rural Telephone Bank (“RTB”) notes payable due quarterly through 2027 at fixed interest rates ranging from 2% to 7.5%. (5.3% weighted average, secured by assets of the telephone companies)	\$ 30,249	\$ 29,305	\$ 26,367
Bank Credit facilities utilized by certain telephone and telephone holding companies due through 2017, at variable interest rates averaging 3.5%	33,043	30,775	24,968
Unsecured notes issued in connection with acquisitions at fixed interest rates averaging 8.3%	36,479	34,781	34,735
Other	1,334	1,328	1,147
	101,105	96,189	87,217
Current maturities	(20,381)	(11,810)	(9,703)
	<u>\$ 80,724</u>	<u>\$ 84,379</u>	<u>\$ 77,514</u>

F. Comprehensive Income

Other comprehensive income, net of tax, which consists of unrealized gains (losses) on available for sale securities, as of September 30, 2011, December 31, 2010 and September 30, 2010 are as follows (in thousands):

	Unrealized Gain (Loss)	Tax Effect	Net
	<i>(in thousands)</i>		
Balance at December 31, 2010	\$ 62	\$ (21)	\$ 41
Unrealized gains (losses) on available for sale securities, net	(24)	8	(16)
Balance at September 30, 2011	<u>\$ 38</u>	<u>\$ (13)</u>	<u>\$ 25</u>
Balance at September 30, 2010	<u>\$ 65</u>	<u>\$ (22)</u>	<u>\$ 43</u>

G. Litigation

The Company’s California subsidiary has been party, along with other small independent telephone companies in California, to a lawsuit against the California Public Utility Commission (“CPUC”). In 2006, the Rural Telephone Bank (“RTB”) was dissolved and accordingly, the holders of its Class B and Class C stock were paid the par value of their stock. In the fourth quarter of 2007, the RTB made a final distribution to holders of its Class B and Class C stock for amounts in excess of par value. The CPUC issued decisions that the intrastate proceeds from the RTB stock dissolution and distribution should benefit the ratepayers of California plus interest on such proceeds. Accordingly, in 2009, the Company accrued a contingent loss of \$0.8 million in Gains (loss) on sale of investments, interest expense of \$0.1 million and recorded a deferred tax benefit of \$0.4 million to recover taxes previously paid. In 2010, additional CPUC rulings resulted in an additional \$0.2 million of interest and penalties. In July 2011, the Appeals Court annulled such CPUC rulings and remanded the case to the CPUC for reallocation in accordance with the Appeals Court ruling. Any reversal of contingent losses recorded in 2009 and 2010 is pending a final CPUC ruling.

LICT is a party to routine litigation incidental to its business. Based on information currently available, the Company believes that none of this ordinary routine litigation, either individually or in the aggregate, will have a material effect on its financial condition and results of operations.

H. Related Party Transactions

At September 30, 2011, December 31, 2010 and September 30, 2010, assets of \$7.6 million, \$12.2 million and \$14.4 million, which are classified as cash and cash equivalents, are invested in United States Treasury money market funds for which an affiliate of the Company's Chairman serve as investment manager to the respective fund.

MANAGEMENT'S DISCUSSION OF OPERATIONS

This discussion should be read together with the Consolidated Financial Statements of LICT Corporation and the notes thereto.

RESULTS OF OPERATIONS

Overview

LICT's telecommunications broadband operations consist of fifteen RLECs, located in California, Iowa, Kansas, Michigan, New Hampshire, New Mexico, New York, Utah and Wisconsin. The RLECs operations range in size from approximately 600 to 6,600 access lines and in addition to telephone service, offer additional services such as Internet service, cable TV service, alarm services, long distance service and competitive local exchange carrier ("CLEC") service.

On March 31, 2010, Sunshine PCS Corporation ("Sunshine") acquired all of the interests of the Company's North Dakota operations ("Sunshine Acquisition"). As consideration, Sunshine issued shares of its Class A common stock reflecting approximately 98% of its outstanding stock, to a subsidiary of the Company. On May 28, 2010, LICT distributed shares of Sunshine (and cash in lieu of fractional shares at the rate of \$50 per share) to its shareholders, spinning off the North Dakota operations to them.

The telecommunications industry in general and the RLECs that comprise LICT's business face a number of economic or industry-wide issues and challenges.

- Regulatory- The Telecommunications Act of 1996 and other federal and state legislation and regulations have a significant impact on the industry and on rural carriers in particular. LICT's telephone companies are all RLECs serving very high cost areas with a significant portion of their revenues being derived from federal or state support mechanisms, which are referred to as Universal Service Funds ("USF"). The revenues and margins of our RLEC subsidiaries are largely dependent on the continuation and level of such support mechanisms.
- Competition- The effects of competition from other telecommunications providers including cable television companies, CLECs, internet, wireless service, and Voice over Internet Protocol ("VoIP") is an industry-wide issue that is felt to varying degrees by our RLECs.
- The economy- Unemployment, building starts, business bankruptcies and the overall health of the economy have a significant effect on demand for our services.
- Market challenges- Our RLECs are required to comply with industry-wide initiatives such as local number portability and the requirements of the Communications Assistance for Law Enforcement Act ("CALEA") that are expensive to implement and that in some cases have limited demand in our markets.

LICT generates cash and earns telecommunications revenues primarily from local network access, intrastate and interstate access revenue and from state and federal USF support mechanisms. The Company's regulated telephone operations, revenues and operating expenses, although relatively stable period to period, are subject to increasing competitive pressures, which gradually reduce revenue and profitability.

- Local Revenues - The number of access lines is the primary driver of local network access revenues. In addition, the ratio of business to residential lines, as well as the number of features subscribed to by customers, are secondary drivers.

- Intrastate access revenues - Customer usage, primarily based on minutes of use, and the number of access lines are the primary drivers of intrastate access revenues since the Company's RLECs are on a "bill-and-keep" basis.
- Interstate Access Revenues - All of our RLECs participate in both the common line and traffic-sensitive National Exchange Carrier Association ("NECA") access pools. Interstate access revenues depend upon whether the RLEC has elected to be "cost-based" or has remained an "average schedule" carrier. The revenues of our ten cost-based carriers directly correlate to the rate-of-return on regulated net investment earned by the NECA access pools plus the interstate portion of regulated operating expenses including taxes. The revenues of the Company's five average schedule subsidiaries are derived based on national formulas with usage based measurements such as access lines, interstate minutes-of-use, and the number and mileage of different types of circuits. The average schedule formulas are intended to be a proxy for cost-based recovery.
- USF subsidies - The primary drivers of USF subsidies are investments in specific types of infrastructure, as well as certain operating expenses and taxes of the Company. Interstate and intrastate USF subsidies are included in the respective interstate and intrastate access revenue captions in the breakdown of revenue and operating expenses which follows.
- Other business revenue - LICT's companies also provide non-regulated telecommunications related services, including Internet access service, wireless and long distance resale service, in certain of its telephone service and adjacent areas. LICT also provides local telephone and other telecommunications service outside certain of its incumbent local exchange carrier ("ILEC") areas with CLEC operations in selected nearby areas. In addition, certain of LICT's companies have expanded into cable TV and security businesses in the areas in which they operate.
- Long Distance revenues are only retained by the Company if it is providing the long distance service to the end user customer as the toll provider. For unaffiliated inter-exchange carriers who contract with LICT for billing services, the Company provides billing services and receives an administrative handling fee as well as access fees for originating and terminating calls.

The following are material opportunities, challenges and risks that LICT's executives are currently focused on, as well as actions that are being taken to address the concerns:

- Universal Service, Intercarrier Compensation and Access Charge Reform - On October 27, 2011, the FCC adopted its Universal Service Fund ("USF") and Intercarrier Compensation ("ICC") Order and Further Notice of Proposed Rulemaking ("FNPRM"). While the Order and FNPRM are not yet released, the Executive Summary released on October 27 provides an overview of the expected changes. In reference to USF, the FCC created the Connect America Fund ("CAF"), which will ultimately replace all existing high-cost support mechanisms. For ICC, the FCC adopted a uniform national bill-and-keep framework as the ultimate end state for all telecommunications traffic exchanged with a LEC. This Order and FNPRM effectuates the requirements put forth in the National Broadband Plan ("NBP") the FCC released to Congress in March 2010, setting the roadmap for achieving universal broadband by 2020. The plan recommends a comprehensive reform of the current universal service mechanisms to support the deployment of broadband including ensuring that low-income Americans can afford broadband. After the details of the FCC Order are released, management will quantify the impact on future USF and ICC revenues.
- Loss of Access Revenues from VoIP and wireless usage - The Company is experiencing revenue losses as usage shifts from landline service provided by the Company's subsidiaries to wireless or VoIP services. VoIP traffic currently does not pay access charges or contribute to universal service, however the FCC's October 27 Order makes clear that VOIP traffic will contribute in the future for use of the underlying network on which the VoIP call travels.

Third quarter ended September 30, 2011 compared to 2010

The following is a breakdown of revenues and operating costs and expenses (in thousands):

	<u>Three months ended September 30,</u>		<u>Increase (Decrease)</u>
	<u>2010</u>	<u>2011</u>	
	(Unaudited)		
Revenues:			
Local access	\$ 2,992	\$ 2,921	\$ (71)
Interstate access	8,808	9,366	558
Intrastate access	2,843	2,681	(162)
Other business	8,071	8,312	241
Total	<u>22,714</u>	<u>23,280</u>	<u>566</u>
Operating Cost and Expense:			
Cost of revenue, excluding depreciation	9,803	10,350	547
General and administrative costs at operations	3,517	3,728	211
Corporate office expenses	963	843	(120)
Depreciation and amortization	4,280	4,410	130
Total	<u>18,563</u>	<u>19,331</u>	<u>768</u>
Operating profit	<u>\$ 4,151</u>	<u>\$ 3,949</u>	<u>\$ (202)</u>

Total revenues in 2011 increased \$0.6 million, or 2.5%, to \$23.3 million compared to \$22.7 million in 2010. Local access revenue decreased \$0.1 million resulting from a 4.0% decrease in access lines offset by the sale of additional services and features. The decrease in access lines is due to the shift by consumers from landline to wireless and VoIP services. VOIP traffic currently does not pay access charges or contribute to universal service. Interstate access revenue increased \$0.6 million in 2011 primarily due a negative true-up in 2010 resulting from cost studies, partially offset by a reduction of minutes of use, and reduced USF funding due to a lower rate base at several of our operations. Intrastate network access revenue decreased \$0.2 million due to a loss of state funding in Kansas due to a state review and a reduction of minutes of use at several of our companies. Other business revenues increased \$0.2 million due to increased broadband and CLEC penetration.

Total costs and expenses were \$19.3 million in 2011, an increase of \$0.8 million compared to 2010. Costs of revenue increased \$0.5 million due to increased costs from the growing internet and cable television operations as well as start up costs for certain CLEC operations. General and administrative costs incurred at the operations increased \$0.2 million. Corporate office expenses were \$0.8 million in 2011, a decrease of \$0.1 million compared to the 2010 quarter. Depreciation and amortization were \$0.1 million higher in the 2011 quarter.

As a result of the above, operating profit in 2011 decreased by \$0.2 million to \$3.9 million compared to \$4.2 million in 2010.

Modified EBITDA

“Modified EBITDA” is a non-GAAP financial measure that we define as net income (loss) before depreciation and amortization expense, interest expense, investment income, equity in earnings of affiliated companies, gain (loss) on sale of investment, impairment charges, income tax expense (benefit), and net income from discontinued operations. Modified EBITDA also includes the actual cash we received from the equity in earnings of affiliated companies. Although we do not have majority voting control of such companies, we have the ability to significantly influence financial and accounting policies. The inclusion of cash received from equity affiliates is a change from past practice which added \$416 and \$381 to the third quarter of 2011 and 2010, respectively and \$1,929 and \$1,050 to the nine months of 2011 and 2010, respectively.

Modified EBITDA is not intended to replace operating income (loss), net income (loss), cash flow and other measures of financial performance and liquidity reported in accordance with accounting principles generally accepted in the United States. Rather, Modified EBITDA is a measure of operating performance and liquidity that investors may consider in addition to such measures. Our management believes that Modified EBITDA is a significant measure of operating performance and liquidity that is commonly reported and widely used by analysts, investors, and other interested parties in the telecommunications industry because it eliminates many differences in financial, capitalization, and tax structures, as well as non-cash and non-operating charges to earnings. We believe that Modified EBITDA trends are a valuable indicator of whether our operations are able to produce sufficient operating cash flow to fund working capital needs, service debt obligations, and fund capital expenditures. We currently use Modified EBITDA for these purposes. We believe that the addition of cash received from equity affiliates further strengthens this measure. Modified EBITDA also is used internally by our management to assess ongoing operations and is a measure used to test compliance with certain covenants of our senior notes, our Revolver and our Term Loan. The definition of EBITDA under our Revolver, our Term Loan and our senior notes differs from the definition of Modified EBITDA used in this table. The definition of EBITDA under our Revolver and Term Loan, discussed below, and senior notes also excludes certain non-cash items. However, the resulting calculation is not materially different from the calculation of Modified EBITDA as defined for the periods presented. Modified EBITDA as used in this document may not be comparable to similarly titled measures reported by other companies due to differences in accounting and disclosure policies.

The following table provides the components of Modified EBITDA and reconciles it to net income from continuing operations:

	<u>Three months ended September 30,</u>		Increase (Decrease)
	<u>2010</u>	<u>2011</u>	
Modified EBITDA from:			
Operating units	\$ 9,395	\$ 9,202	\$ (193)
Cash distributions – equity companies	381	416	35
Total before corporate expenses	<u>9,776</u>	<u>9,618</u>	<u>(158)</u>
Corporate expense	(963)	(843)	120
Modified EBITDA	<u>\$ 8,813</u>	<u>\$ 8,775</u>	<u>\$ (38)</u>
 Reconciliation to net income:			
Modified EBITDA	\$ 8,813	\$ 8,775	\$ (38)
Less cash distributions – equity companies (see above)	(381)	(416)	(35)
Depreciation and amortization	(4,280)	(4,410)	(130)
Investment income	34	27	(7)
Interest expense	(1,787)	(1,551)	236
Equity in income of affiliates	774	1,028	254
Gain on sale of investments	216	--	(216)
Income tax	<u>(1,339)</u>	<u>(1,345)</u>	<u>(6)</u>
Net income from continuing operations	<u>\$ 2,050</u>	<u>\$ 2,108</u>	<u>\$ 58</u>

Other Income (Expense)

In 2011, investment income decreased slightly primarily due to lower cash balances and interest rates.

Interest expense decreased by \$0.2 million in 2011 due primarily to a reduction in debt outstanding due to scheduled debt repayments.

Equity in earnings of affiliates in 2011 increased by \$0.3 million due to significant growth in a 25% owned cellular telephone partnership in California.

Income Tax Provision

The income tax provision includes federal, as well as state and local taxes. The tax provision for 2011 and 2010, represent effective tax rates of 39.0% and 39.5%, respectively. The difference between these effective rates and the federal statutory rate is principally due to state income taxes.

Net Income from continuing operations

Net income from continuing operations in the third quarter of 2011, was \$2.1 million, or \$89.11 per share (basic and diluted), compared to a net income last year of \$2.1 million, or \$84.51 per share (basic and diluted). The Company has no dilutive instruments outstanding.

Nine months ended September 30, 2011 compared to 2010

The following is a breakdown of revenues and operating costs and expenses (in thousands):

	<u>Nine months ended September 30,</u>		<u>Increase</u>
	<u>2010</u>	<u>2011</u>	<u>(Decrease)</u>
	(Unaudited)		
Revenues:			
Local access	\$ 9,028	\$ 8,689	\$ (339)
Interstate access	28,756	27,257	(1,499)
Intrastate access	8,596	7,829	(767)
Other business	22,885	24,374	1,489
Total	<u>69,265</u>	<u>68,149</u>	<u>(1,116)</u>
Operating Cost and Expense:			
Cost of revenue, excluding depreciation	28,758	29,973	1,214
General and administrative costs at operations	10,602	10,689	87
Corporate office expenses	2,712	2,409	(303)
Depreciation and amortization	12,913	12,804	(109)
Total	<u>54,986</u>	<u>55,875</u>	<u>889</u>
Operating profit	<u>\$ 14,279</u>	<u>\$ 12,274</u>	<u>\$ (2,005)</u>

Total revenues in 2011 decreased \$1.1 million, or 1.6%, to \$68.1 million compared to \$46.6 million in 2010. Local access revenue decreased \$0.3 million resulting from a 4.0% decrease in access lines offset by the sale of additional services and features. The decrease in access lines is due to the shift by consumers from landline to wireless and VoIP services. VOIP traffic currently does not pay access charges or contribute to universal service. Interstate access revenue decreased \$1.5 million in 2011 primarily due to a reduction of minutes of use, reduced USF funding due to a lower rate base at several of our operations and by \$0.5 million of additional interstate out of period adjustment revenue in the 2010 period. Intrastate network access revenue decreased \$0.8 million due to a loss of state funding in Kansas resulting from a state review and a reduction of minutes of use at several of our companies. Other business revenues increased \$1.5 million due to increased broadband and CLEC penetration.

Total costs and expenses were approximately \$55.9 million in the 2011 period, compared to \$55.0 million in 2010. Costs of revenue increased \$1.2 million primarily due to increased costs from the growing internet and cable television operations as well as start up costs for certain CLEC operations. General and administrative costs incurred at the operations increased \$0.1 million. Corporate office expenses decreased \$0.3 million. Depreciation and amortization decreased by \$0.1 million.

As a result of the above, operating profit in 2010 decreased by \$2.0 million to \$12.3 million compared to \$14.3 million in 2010.

The following table provides the components of Adjusted Operating Profit and reconciles it to net income from continuing operations:

	<u>Nine months ended September 30,</u>		Increase (Decrease)
	<u>2010</u>	<u>2011</u>	
Modified EBITDA from:			
Operating units	\$ 29,904	\$ 27,487	\$ (2,417)
Cash distributions – equity companies	1,050	1,929	879
Total before corporate expenses	<u>30,954</u>	<u>29,416</u>	<u>(1,538)</u>
Corporate expense	<u>(2,712)</u>	<u>(2,409)</u>	<u>303</u>
Modified EBITDA	<u>\$ 28,242</u>	<u>\$ 27,007</u>	<u>\$ (1,235)</u>
 Reconciliation to net income:			
Modified EBITDA	\$ 28,242	\$ 27,006	\$ (1,235)
Less cash distributions – equity companies (see above)	(1,050)	(1,929)	(879)
Depreciation and amortization	(12,913)	(12,804)	109
Investment income	1,016	756	(260)
Interest expense	(5,364)	(4,891)	473
Equity in income of affiliates	1,386	2,145	759
Gain on sale of investments	216	--	(216)
Income tax	<u>(4,606)</u>	<u>(4,244)</u>	<u>362</u>
Net income from continuing operations	<u>\$ 6,927</u>	<u>\$ 6,040</u>	<u>\$ (887)</u>

Other Income (Expense)

In 2011, investment income decreased by \$0.3 million primarily due to lower cash balances and interest rates, offset by higher dividends from investments.

Interest expense decreased by \$0.5 million in 2011. Interest expense was \$0.4 million lower due to a reduction in debt outstanding due to scheduled debt repayments. In addition, the 2010 period included a \$0.1 million write-off of unamortized debt issuance cost due to the pay-off of the remaining balance of a note with a bank on March 31, 2010.

Equity in earnings of affiliates in 2011 increased by \$0.8 million primarily due to increased earnings from our 25% partnership interest in a cellular telephone provider in California.

Income Tax Provision

The income tax provision includes federal, as well as state and local taxes. The tax provision for 2011 and 2010, represent effective tax rates of 41.3% and 39.9%, respectively. The difference between these effective rates and the federal statutory rate is principally due to state income taxes and in 2011, includes an income tax provision of \$0.2 million resulting from a taxable gain on the sale of a life insurance policy, with no corresponding pre-tax book income.

Net Income from continuing operations

Net income from continuing operations in the first nine months of 2011 was \$6.0 million, or \$253.15 per share (basic and diluted), compared to a net income last year of \$6.9 million, or \$285.36 per share (basic and diluted). The Company has no dilutive instruments outstanding.

LIQUIDITY AND CAPITAL RESOURCES

Liquidity

The debt at LICT's subsidiary companies contains restrictions on the amount of funds that can be transferred to their respective parent companies. LICT receives cash to meet its obligations primarily through management fees charged to its subsidiaries, dividends, a tax sharing agreement with its subsidiaries, usage of a line of credit facility, and has obtained additional liquidity by refinancing certain subsidiary debt and by the sale of assets.

The Company's \$17.5 million line of credit facility with a bank will decrease by \$0.6 million quarterly starting June 30, 2012, with the remaining \$12.7 million due on June 30, 2014. Interest on borrowings will be at LIBOR plus 5.5%. Management believes such extension provides adequate liquidity for at least the next twelve months. Outstanding under the line of credit facility, classified in notes payable to banks, was \$14.5 million, \$15.7 million and \$13.3 million at September 30, 2011, December 31, 2010 and September 30, 2009, respectively.

On March 31, 2010, LICT utilized \$7.4 million of its line of credit to pay-off the remaining balance of a loan with a bank at Lynch Telephone North that was partially secured by the assets of Lynch Telephone II, LLC, a subsidiary of LICT. Such loan pay-off was made in order to effectuate the Sunshine Acquisition of all of the interests of Lynch Telephone II, which owns 100% of Inter-Community Telephone Company, LLC and Valley Communications, Inc. Inter-Community is a rural independent local telephone company ("RLEC") serving communities in southeastern North Dakota providing regulated telephone service and Valley provides internet and other non-regulated services. As consideration, Sunshine issued shares of its Class A common stock reflecting approximately 98% of its outstanding stock, to Lynch Telephone North L.L.C., the parent company of Lynch Telephone II. On May 28, 2010, the Company distributed almost all of the Sunshine Class A shares to its shareholders in the form of a dividend.

LICT was awarded, and is in process of completing documentation to receive \$6.5 Million of grant and \$1.0 Million of loan stimulus funds from the Department of Agriculture's Rural Utilities Service ("RUS") Broadband Initiatives Program. This funding is aimed at expanding broadband access in unserved and underserved portions of the nation. LICT will expand and upgrade broadband service at four of our Telephone Companies, in New Hampshire, Kansas, California and Utah, with this stimulus funding with work expected to be completed later in 2011 or 2012. As of September 30, the Company has spent approximately \$0.8 million more than funding received, which is included in other current assets.

The Company is obligated under long-term debt provisions and lease agreements to make certain cash payments over the term of the agreements. The following table summarizes, as of September 30, 2011 for the periods shown, these contractual obligations and certain other financing commitments from banks and other financial institutions that provide liquidity:

	Payments Due by Period				
	(In thousands)				
	Total	Less than 1 year	1 – 3 years	4 – 5 years	After 5 years
Long-term debt, principal only	\$ 87,217	\$ 9,703	\$ 34,006	\$ 18,229	\$ 25,279
Operating leases	4,475	693	1,209	1,122	1,451
Notes payable to banks, principal only	14,535	--	14,535	--	--
Interest on debt and notes	21,342	5,983	9,170	4,115	2,074
Total contractual cash obligations and commitments	\$ 127,569	\$ 16,379	\$ 58,920	\$ 23,466	\$ 28,804

At September 30, 2011, total debt (including notes payable to banks) was \$101.8 million, a decrease of \$10.1 million from December 31, 2010. At September 30, 2011, there was \$62.2 million of fixed interest rate debt outstanding, averaging 7.0%, and \$39.6 million of variable interest rate debt, averaging 4.7%. The debt at fixed interest rates includes \$34.7 million of subordinated notes at interest rates averaging 8.3% issued to sellers as part of acquisitions. The long-term debt facilities at certain subsidiaries are secured by substantially all of such subsidiaries' assets, while at other subsidiaries it is secured by the common stock

of such subsidiaries. In addition, the debt facilities contain certain covenants restricting distributions to LICT. Substantially all of the subsidiaries' net assets are restricted.

LICT has a manageable degree of financial leverage. As of September 30, 2011, the ratio of total debt to Modified EBITDA, on a trailing twelve month basis, was 2.9 to 1. Certain subsidiaries have higher debt to Modified EBITDA ratios.

As of September 30, 2011, LICT had current assets of \$25.5 million and current liabilities of \$35.2 million resulting in negative working capital of \$9.6 million compared to negative \$10.3 million at December 31, 2010.

Sources and Uses of Cash

Cash at September 30, 2011, was \$11.5 million, a decrease of \$3.7 million compared to December 31, 2010. In the first nine months of 2011, net cash provided by operations of \$19.3 million was primarily used to invest in plant and equipment and repay debt.

Capital expenditures were \$11.2 million in the first nine months of 2011 compared to \$10.3 million in 2010, which are predominantly spent at the RLECs and, for our cost based companies, will be included in their rate bases for rate setting purposes.

In 2008 through 2010, the Company has taken bonus depreciation deductions for eligible property additions as allowed by the Internal Revenue Service of 50%, starting January 1, 2008 and 100%, starting September 9, 2010. Such deductions which have the effect of reducing current taxes payable, will continue at 50% through 2012, but will increase tax payments in future years.

In May 2011, the Company sold a life insurance policy, for its cash surrender value, on a former owner of one of our operating companies, thereby unlocking \$1.6 million of liquidity.

On May 20, 2010, the Company purchased a cable communications company providing cable television, broadband and voice telephone services to approximately 1,700 customers in rural communities throughout southeastern Kansas for \$2.1 million in cash. The operations will complement an existing CLEC business as well as one of our RLEC operations in southeastern Kansas. Such cable company had previously been owned by a subsidiary of LICT, and was spun off from LICT as part of the spin-off of CIBL Inc. in November 2007.

The company is considering a significant refinancing initiative which will enhance our ability to take the operational steps necessary to position the organization for future success. The Company is currently weighing its options in this regard and the implementation of this refinancing will be predicated on its ability to obtain acceptable terms.

The Company's Board of Directors has authorized the purchase of up to 3,000 shares of the Company's common stock and in September 2011 authorized an additional 1,000 shares. The Company's bank covenants, however, further restrict share repurchases. Through September 30, 2011, 3,064 shares allowed under the bank covenants had been purchased at an average investment of \$2,986 per share, including 406 shares purchased in 2011 at an average investment of \$2,253 per share. In October 2011, an additional 35 shares were repurchased for an average investment of \$2,141 per share.

The Company has not paid any cash dividends since its inception in 1999.