

LYNCH INTERACTIVE CORPORATION

BUSINESS

Lynch Interactive Corporation ("Interactive" or the "Company") was incorporated in 1996 under the laws of the State of Delaware. On September 1, 1999, Interactive was spun off by Lynch Corporation to its shareholders (the "Spin Off") and became a public company. As a successor to certain businesses of Lynch Corporation, Interactive, at that time, became a diversified holding company with subsidiaries primarily engaged in multimedia and transportation services. Interactive spun off its ownership interest in Sunshine PCS to its shareholders in 2001 and its 63% interest in the Morgan Group, Inc. to its shareholders in 2002. Interactive's executive offices are located at 401 Theodore Fremd Avenue, Rye, New York 10580-1430. Its telephone number is 914-921-8821.

Interactive's business development strategy is to expand its existing operations through internal growth and acquisitions. It may also, from time to time, consider the acquisition of other assets or businesses that are not related to its present businesses. The Company currently operates in one business segment, multimedia, which consists of telecommunications, alarm services, cable television and broadcasting. As used herein, Interactive includes subsidiaries.

Lynch Interactive Corporation delists and goes to what Wall Street refers to as "Pink Sheets", and others refer to as "Going Dark"

On November 10, 2005 the Company concluded a one-for-hundred reverse stock split as part of a "going dark" transaction, which was approved by the shareholders on October 31, 2005 and by the Board of Directors on November 3, 2005. Under the terms of this transaction, holders of less than 100 shares received cash in lieu of fractional shares at a rate of \$29.9352 per (pre-split) shares. As part of the transaction the Company voluntarily delisted from the American Stock Exchange ("AMEX") on December 22, 2005 and filed a Form 15 with the Securities and Exchange Commission ("SEC") deregistering its shares. The Form 15 was filed on December 23, 2005 and the Company is no longer a reporting company under the Securities Exchange Act of 1934.

The Company's shares are quoted on the Pink Sheets[®] under the symbol "LICT". The Company has approximately 150 record holders and intends to disseminate quarterly and annual financial statements and press releases to the financial community.

The principal reason for taking this step was the cost required to comply with section 404 of the Sarbanes-Oxley Act of 2002. While the Company is committed to having a system of controls in place and consistently improving those controls necessary to generate reliable financial statements, the documentation and testing process required by section 404 of Sarbanes-Oxley would likely impose considerable costs and a staffing strain on the Company and its subsidiaries unless the standards are revised for smaller companies.

MULTIMEDIA OPERATIONS

Wireline Telecommunications

Operations. Interactive conducts its telecommunications operations through subsidiary companies. The telecommunications group has been expanded through the selective acquisition of local exchange telephone companies serving rural areas and by offering additional services such as Internet service, alarm services, long distance service and competitive local exchange carrier service. Since 1989, Interactive has acquired fifteen telephone companies, two of which have indirect minority ownership of 19%, whose operations range in size from approximately 900 to over 10,000 access lines. The Company's telephone operations are located in California, Iowa, Kansas, Michigan, New Hampshire, New Mexico, New York, North Dakota, Utah and Wisconsin. Our service areas are largely residential and not densely populated. As of December

31, 2005, total lines, including both access and DSL, were 59,695, 100% of which are served by digital switches.

On August 29, 2005, the Company acquired 100% of the stock of California-Oregon Telecommunications Company ("Cal-Ore") located in Dorris, California for \$21.5 million, including acquisition costs. Cal-Ore's subsidiary Cal-Ore Telephone Company is the incumbent service provider for a rural area of about 850 square miles along the Northern California border with Oregon with approximately 2,500 access lines. Cal-Ore's other businesses include an Internet service provider, Competitive Local Exchange Carrier ("CLEC"), that is planning to provide services in the surrounding area, and minority interests in two cellular partnerships, one of which was sold in February 2006.

Principal Products and Services. The principal business of Interactive's telephone companies is to provide telecommunications services. These services fall into three major categories:

Local network services. We provide telephone wireline access services to residential and non-residential customers in our service areas. We provide our local network customers a number of calling features including call forwarding, conference calling, caller identification, voicemail and call waiting. We offer packages of telecommunications services. These packages permit customers to bundle their basic telephone line with their choice of enhanced services, or to customize a set of selected enhanced features that fit their specific needs.

Network access services. We provide network access services to long distance carriers and other carriers in connection with the use of our facilities to originate and terminate interstate and intrastate telephone calls. Such services are generally offered on a month-to-month basis and the service is billed on a minutes-of-use basis. Access charges to long distance carriers and other customers are based on access rates filed with the Federal Communications Commission ("FCC") for interstate services and with the respective state regulatory agency for intrastate services.

Other Business. Interactive also provides non-regulated telephone-related services, including Internet access service and long distance resale service in certain of its telephone service (and adjacent) areas. Interactive also provides and intends to provide more local telephone and other telecommunications service outside certain of its franchise areas by establishing CLEC operations in certain nearby areas. In selected areas, Interactive provides security installation and monitoring services to homes and businesses and cable television services ("CATV").

Product Status. The Company is always trying to roll out new services based on technological advances. We expect future growth in telephone operations to be derived from the acquisition of additional telephone companies, from providing service to new customers or additional services to existing customers, from upgrading existing customers to higher grades of service, and from new service offerings. Interactive is currently providing Voice over Internet Protocol ("VoIP") on a limited basis and is exploring options for expanding such service.

The following table summarizes certain information regarding Interactive's multimedia operations:

	Years Ended December 31,		
	2003	2004	2005
<u>Telecommunications operations</u>			
Access lines (a)	52,517	50,803	53,015
DSL Lines	2,709	4,098	6,680
Total access lines	55,226	54,901	59,695
% Residential	73%	76%	76%
% Business	27%	24%	24%
Internet subscribers (including DSL)	20,853	20,240	20,078
Cable subscribers	2,731	3,630	5,996

Total Multimedia Revenues

Local service	14%	13%	13%
Network access	62%	63%	62%
Other businesses	24%	25%	25%
Total multimedia revenues	<u>100%</u>	<u>100%</u>	<u>100%</u>

- (a) An "access line" is a telecommunications circuit between the customer's establishment and the central switching office.
- (b) Other Businesses includes Internet, alarm services, CLEC, CATV and other non-regulated revenues.

Telephone Acquisitions. Interactive pursues an active program of acquiring operating telephone companies. Since 1989, Interactive acquired fourteen telephone companies serving a total of approximately 45,600 access lines, at the time of these acquisitions, for an aggregate consideration totaling approximately \$153.6 million. Such acquisitions are summarized in the following table:

	Year of Acquisition	Number of Access Lines Yr. Of Acq.	Number of Access Lines 12/31/05	Ownership Percentage
Western New Mexico Telephone Co.	1989	4,200	7,000	83.1 ^(c)
Inter-Community Telephone Co.	1991	2,550 ^(a)	2,501	100.0
Cuba City Telephone Co. & Belmont Telephone Co.	1991	2,200	2,533	81.0
Bretton Woods Telephone Co.	1993	250	908	100.0
JBN Telephone Co.	1993	2,300 ^(b)	2,587	98.0
Haviland Telephone Co.	1994	3,800	3,585	100.0
Dunkirk & Fredonia Telephone Co. & Cassadaga Telephone Co.	1996	11,100	11,286	100.0
Upper Peninsula Telephone Co.	1997	6,200	7,080	100.0
Central Scott Telephone Co.	1999	6,000	5,761	100.0
Central Utah Telephone Co./Skyline Telephone Company/Bear Lake Telephone Company	2001	7,000	7,217	100.0
California-Oregon Telephone Co.	2005	2,500	2,557	100%

- (a) Includes 1,350 access lines acquired in 1996.
- (b) Includes 354 access lines acquired in 1996.
- (c) Does not include a 36% interest in a company that owns the 16.9% minority interest. In January 2006, the Company acquired the remaining minority interest.

Interactive continually evaluates acquisition opportunities targeting domestic rural telephone companies with a strong market position, good growth potential and predictable cash flow. In addition, Interactive generally seeks companies with excellent local management already in place who will remain active with their company. At times, certain large telephone companies have offered certain of their rural telephone exchanges for sale, often on a statewide or larger area basis. Interactive has and in the future may, bid on such groups of exchanges. Telephone holding companies and others actively compete for the acquisition of telephone companies and such acquisitions are subject to the consent or approval of regulatory agencies in most states. While management believes it will be successful in making additional acquisitions, any acquisition program is subject to various risks, including being able to find and complete acquisitions at an attractive price and being able to integrate and operate successfully any acquisition made.

Related Services and Investments. Fifteen of Interactive's telephone companies now offer Internet access service, either directly or through affiliated companies. At December 31, 2005, Internet access customers totaled 20,078 compared to 19,387 at December 31, 2004. Interactive companies have increased DSL

customers offset by a decrease in dial up service. Affiliates of six of Interactive's telephone companies now offer long distance service, and affiliates of three of Interactive's telephone companies now offers CLEC services. Several more are in the process of setting up long distance, Voice over Internet Protocol (VoIP), and CLEC operations.

An affiliate of Dunkirk & Fredonia Telephone Company ("DFT") provides CLEC service on a resale basis in neighboring Dunkirk, New York, certain areas of Buffalo, New York, and two other western New York counties. Some of DFT's CLEC services are being provided via an unbundled network elements platform (UNE-P), which allows for increased margins over a resale CLEC business model. In addition, in 2005 DFT started offering VoIP and CLEC services through their own facilities.

Giant Communications Inc. provides CLEC services in Northeast Kansas and is beginning to provide VoIP services to end users.

Giant Communications LLC (formerly CLR Video, L.L.C.), a 98% owned subsidiary of Interactive, is a provider of cable television in northeast Kansas with approximately 2,400 subscribers.

CS Technologies, Inc. provides CLEC services, as well as VoIP and other data services, in Mount Joy, Bettendorf and Davenport, Iowa through their own facilities.

Central Telcom Services, LLC ("CTS"), a 100% owned subsidiary of the Company based in Fairview, Utah, acquired two cable television systems in February 2004 and March 2005 serving twenty counties. The Company is providing cable modem service in two communities and is in the process of rebuilding additional systems to provide two-way service. As of December 31, 2005, CTS had 3,603 cable TV subscribers and 160 cable modem customers. These acquisitions position the company to promote additional services to its customer base.

DFT Security Systems, Inc. (which is 63.6% owned by Interactive), another affiliate of DFT, acquired American Alarm Company in December 2001. DFT Security Systems provides alarm services to western New York, including the Buffalo area. In 2005, the Company sold 6x% of its customer accounts to an investment company for which the Company continues to act as a service provider. At December 31, 2005, the Company serves 2,164 customers in addition to those for which it is the service provider.

A subsidiary of Inter-Community Telephone Company in North Dakota, and Western New Mexico Telephone Company in New Mexico have filed with their respective state regulatory commissions to provide CLEC services in those states. In addition, CTS has obtained approval to operate as a CLEC in Nevada and is in the process of obtaining approval to establish CLEC operations in Utah. Final plans to offer CLEC service in areas adjacent to Interactive's telephone operations in those states have not been completed. There is no assurance that Interactive can successfully develop these businesses or that these new or expanded businesses can be made profitable within a reasonable period of time. Such businesses, in particular any CLEC business, would be expected to operate at losses initially and for a period of time.

Regulatory Environment. Operating telephone companies are regulated by state regulatory agencies with respect to intrastate telecommunications services and the FCC with respect to interstate telecommunications services.

Telecommunications Act of 1996. In recent years, various aspects of federal and state telephone regulation have been subject to re-examination and on-going modification. In February 1996, the Telecommunications Act of 1996 (the "1996 Act"), which is the most substantial revision of communications regulations since the 1930's, became law. The 1996 Act is intended generally to allow telephone, cable, broadcast and other telecommunications providers to compete in each other's businesses, while loosening regulation of those businesses. Among other things, the 1996 Act (i) allows major long distance telephone companies and cable television companies to provide local exchange telephone service; (ii) allows new local telephone service providers to connect into existing local telephone exchange networks and purchase services at wholesale rates for resale; (iii) provides for a commitment to universal

service for high-cost, rural areas and authorizes state regulatory commissions to consider their status on certain competition issues; (iv) allows the Regional Bell Operating Companies to offer long distance telephone service and enter the alarm services and electronic publishing businesses; (v) removes rate regulation over non-basic cable service; and (vi) increases the number of television stations that can be owned by one party. The 1996 Act had dual goals of fostering local and intrastate competition while ensuring universal service to rural America.

National Exchange Carrier Association. For interstate services, Interactive's telephone subsidiaries participate in the National Exchange Carrier Association ("NECA") common line and traffic sensitive tariffs and access revenue pools. Where applicable, Interactive's subsidiaries also participate in similar pooling arrangements approved by state regulatory authorities for intrastate services. Such interstate and intrastate arrangements are intended to compensate local exchange carriers ("LECs"), such as Interactive's operating telephone companies, for the costs, including a fair rate-of-return, of facilities furnished in originating and terminating interstate and intrastate long distance services.

In addition to access pool participation, certain of Interactive's subsidiaries are compensated for their intrastate costs through billing and keeping intrastate access charge revenues (without participating in an access pool). Intrastate access charge revenues are based on intrastate access rates filed with the state regulatory agency.

Intercarrier Compensation Reform. The FCC released a Further Notice of Proposed Rulemaking ("FNPRM") on March 3, 2005 to examine all aspects of intercarrier compensation including access charges, reciprocal compensation, transport and transiting services, as well as, various network interconnection issues. Currently, the rate for intercarrier compensation depends on the type of traffic at issue, the types of carriers involved, and the end points of the communication. Many believe these rate differentials create both opportunities for regulatory arbitrage and incentives for inefficient investment and deployment decisions. The intent of this proceeding is to replace the existing patchwork of intercarrier compensation rules with a unified approach.

Universal Service Fund. The FCC has completed numerous regulatory proceedings required to implement the 1996 Act. For certain issues, the FCC bifurcated the proceedings between price-cap and rate-of-return companies or in the case of the Universal Service Fund ("USF") mechanisms between rural and non-rural companies. All of Interactive's telephone subsidiaries are rural, rate-of-return companies for interstate regulatory purposes. Rate-of-return companies receive support based on their costs while price cap companies receive support based on the prices of communications services. USF is intended, among other things, to provide special support funds to high cost rural LECs so that they can provide affordable services to their customers, notwithstanding their high cost due to low population density.

On February 25, 2005, the FCC adopted measures addressing the minimum requirements for a telecommunications carrier to be designated as an eligible telecommunications carrier ("ETC") and thus be eligible to receive federal USF. All of Interactive's companies are already designated as ETCs. New carriers seeking ETC designation must now:

- Provide a five-year plan demonstrating how high-cost universal service support will be used to improve its coverage, service quality or capacity throughout the service area for which it seeks designation.
- Demonstrate its ability to remain functional in emergency situations.
- Demonstrate that it will satisfy consumer protection and service quality standards.
- Offer local usage plans comparable to those offered by the incumbent local exchange carrier ("ILEC") in the areas for which it seeks designation.