Pay Tel Communications, Inc.

FINANCIAL STATEMENTS
and Independent Auditor's Report

December 31, 2016 and 2015

Leeper, Kean & Rumley, L.L.P.
Certified Public Accountants and Consultants

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors and Stockholders
Pay Tel Communications, Inc.
Greensboro, North Carolina

Report on the Financial Statements

We have audited the accompanying financial statements of Pay Tel Communications, Inc. (an S Corporation), which comprise the balance sheets as of December 31, 2016 and 2015, and the related statements of operations and retained earnings and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Pay Tel Communications, Inc. as of December 31, 2016 and 2015, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Leeper, Kleen & Rumley, L.L.P.

Greensboro, North Carolina
April 17, 2017

Pay Tel Communications, Inc.

BALANCE SHEETS
December 31, 2016 and 2015

Assets

	2016	2015
Current assets:		
Cash	$ 1,321,428	1,026,862
Net accounts receivable	824,517	689,282
Prepaid expenses and other receivables	301,797	215,259
Related party notes receivable and advances	308,563	396,085
Total current assets	2,756,305	2,327,488
Property and equipment, at cost:		
Inmate communications equipment	5,206,311	4,866,971
Office furniture, equipment and software	7,894,093	7,617,840
Leasehold improvements	1,788,224	1,788,224
Vehicles	683,242	598,158
Total property and equipment	15,571,870	14,871,193
Less accumulated depreciation and amortization	(10,115,386)	(8,637,534)
Net property and equipment	5,456,484	6,233,659
Other assets:		
Net deferred contract costs and commissions	425,761	493,829
Settlement reserve deposits	76,099	83,926
Cash surrender value of Stockholder's life insurance	57,269	57,692
Deposits and other noncurrent assets	1,312	2,350
Total other assets	560,441	637,797
Total Assets	$ 8,773,230	9,198,944

See notes to financial statements.

Pay Tel Communications, Inc.

BALANCE SHEETS
December 31, 2016 and 2015

Liabilities and Stockholders' Equity

	2016	2015
Current liabilities:		
Current portion of equipment loans	$ 356,510	483,530
Current portion of capitalized lease	130,800	31,702
Accounts payable	2,311,957	2,918,246
Accrued expenses and other liabilities	616,598	660,444
Unearned revenues	1,152,812	1,138,432
Due to stockholder	352,663	254,041
Total current liabilities	4,921,340	5,486,395
Noncurrent liabilities:		
Noncurrent portion of equipment loans	602,601	958,291
Noncurrent portion of capitalized lease	117,011	34,375
Total noncurrent liabilities	719,612	992,666
Total liabilities	5,640,952	6,479,061
Stockholders' equity:		
Common stock, 1,000 voting shares and 99,000 nonvoting shares authorized, issued and outstanding	22,500	22,500
Retained earnings	3,109,778	2,697,383
Total stockholders' equity	3,132,278	2,719,883
Total Liabilities and Stockholders' Equity	$ 8,773,230	9,198,944

See notes to financial statements.

Pay Tel Communications, Inc.

STATEMENTS OF OPERATIONS AND RETAINED EARNINGS
For the Years Ended December 31, 2016 and 2015

	2016	2015
Net revenues	$ 27,049,939	27,502,010
Costs of revenues	(15,380,054)	(16,035,140)
Gross profit	11,669,885	11,466,870
Selling, general and administrative expenses:		
Salaries and related expenses	(5,769,143)	(5,448,680)
Professional services	(1,743,060)	(1,471,432)
Depreciation and amortization	(838,158)	(933,682)
Rents, maintenance and utilities	(833,552)	(843,949)
Property taxes, licenses and insurance	(313,911)	(321,833)
Travel	(356,507)	(377,806)
Computer supplies and support	(338,775)	(372,601)
Telephone and broadband	(353,226)	(332,860)
Publications, postage and printing	(179,076)	(180,976)
Marketing	(167,357)	(166,129)
Charitable contributions	(140,089)	(71,246)
Other	(102,493)	(119,305)
Total selling, general and administrative expenses	(11,135,347)	(10,640,499)
Income before other expenses	534,538	826,371
Other income (expenses):		
Florida sales and use tax (Note 11)	200,000	(200,000)
Other income	-	15,853
Loss on related party notes receivable	(61,182)	(54,917)
Interest and amortization	(55,377)	(18,453)
Net loss on disposal of property and equipment	(12,850)	(18,323)
Net other income (expenses)	70,591	(275,840)
Net income	605,129	550,531
Retained earnings at beginning of year	2,697,383	3,168,305
Distributions to stockholders	(192,734)	(1,021,453)
Retained earnings at end of year	$ 3,109,778	2,697,383

See notes to financial statements.

Pay Tel Communications, Inc.

STATEMENTS OF CASH FLOWS
For the Years Ended December 31, 2016 and 2015

Increase (Decrease) in Cash

	2016	2015
Operating activities:		
Net income	$ 605,129	550,531
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of property and equipment	1,722,263	1,482,006
Amortization of deferred contract costs	284,835	452,838
Amortization of other noncurrent assets	4,188	6,587
Allowance for doubtful accounts and other noncash activities	(20,232)	15,232
Impairment of inmate communications equipment	487,341	-
Net loss on disposal of property and equipment	12,850	18,323
Loss on related party notes receivable	61,181	54,917
Cash surrender value of Stockholder's life insurance	423	(834)
(Increase) decrease in related assets:		
Accounts receivable and settlement reserve deposits	(107,176)	(85,599)
Prepaid expenses and other receivables	(86,538)	42,468
Net deferred contract costs	(216,767)	(393,397)
Increase (decrease) in related liabilities:		
Accounts payable	(606,289)	127,448
Accrued expenses and other liabilities	(43,846)	45,404
Unearned revenues	14,380	75,475
Net cash provided by operating activities	2,111,742	2,391,399
Investing activities:		
Purchases of property and equipment	(1,170,722)	(2,403,844)
Net proceeds from sale of property and equipment	23,067	16,097
Net related party advances and due to stockholder	124,963	(26,341)
Net cash used in investing activities	$ (1,022,692)	(2,414,088)

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See notes to financial statements.

Pay Tel Communications, Inc.

STATEMENTS OF CASH FLOWS - CONTINUED
For the Years Ended December 31, 2016 and 2015

	2016	2015
Financing activities:		
Borrowings from equipment loans	$ -	1,190,000
Repayments on equipment loans	(482,710)	(305,775)
Payments on capitalized lease	(115,890)	(29,030)
Distributions to stockholders	(192,734)	(1,021,453)
Loan origination fees	(3,150)	(3,550)
Net cash used in financing activities	(794,484)	(169,808)
Net increase (decrease) in cash	294,566	(192,497)
Cash at beginning of year	1,026,862	1,219,359
Cash at end of year	$ 1,321,428	1,026,862

Supplemental Disclosures

Interest paid	$ 51,000	12,000

Noncash Investing and Financing Activities

During 2016 and 2015, the Company had noncash financing transactions relating to capitalized equipment leases totaling $297,624 and $95,107, respectively.

(1) Nature of Business

Pay Tel Communications, Inc. (the "Company") owns and operates automated telephone communication systems in confinement facilities for use by inmates under contracts with the confinement facilities that typically range from three to five years and expire at various times beginning in 2017**.** The Company services its customers throughout the United States from its headquarters in Greensboro, North Carolina.

(2) Summary of Significant Accounting Policies

(a) Revenue Recognition - Generally, revenues from automated calls from confinement facilities are recognized, net of applicable sales taxes, at the time the call is completed. State and federal regulatory authorities govern certain rates the Company can charge customers for these services.

The majority of customers establish an electronic account through prepayments to the Company. When an electronic account becomes inactive, the Company either refunds the customer's unused balance or issues them a prepaid phone card that does not expire. At any time in the future, customers may use the prepaid phone card or return it to the Company for a refund. The Company recognizes into net revenues the balances of prepaid phone cards that show no activity for at least six months and which the Company believes, based upon historical redemption patterns, the likelihood of redemption by the customer is remote.

(b) Credit Risk - Cash and accounts receivable are financial instruments which potentially subject the Company to credit risk. At various times throughout the year, the Company had cash on deposit with a bank which exceeded the $250,000 federally-insured limit. Management reviews outstanding receivable accounts on an ongoing basis, writes off the amounts deemed uncollectible and provides an additional reserve for uncollectible accounts based on past experience. Total allowances for doubtful accounts receivable accounts at December 31, 2016 and 2015 were approximately $900 and $21,100.

(c) Advertising costs - The Company expenses advertising costs as they are incurred. Advertising expenses for the years ended December 31, 2016 and 2015 were approximately $167,000 and $166,000, respectively.

(d) Property and Equipment - Property and equipment are recorded at cost. Leasehold improvements are depreciated over estimated useful lives ranging from 7 to 39 years using the straight-line method for financial reporting purposes. All other property and equipment are depreciated over estimated useful lives ranging from 3 to 10 years using the straight-line method for financial reporting purposes.

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(e) Net Deferred Contract Costs and Commissions - Net deferred contract costs and commissions consist of payments to Company employees, inmate facilities and other third party providers related to the procurement of certain inmate contracts. Deferred contract costs and commissions are amortized over the lives of the respective contracts. Accumulated amortization at December 31, 2016 and 2015 was $514,565 and $495,167, respectively.

The estimated future amortization expenses related to these deferred costs are as follows:

For the year ending December 31, 2017	$ 222,000
2018	96,000
2019	68,000
2020	26,000
2021	13,500
Thereafter	261
Total maturities	$ 425,761

(f) Income Taxes - The Company, with the consent of its stockholders (“Stockholders”), has elected under the Internal Revenue Code to be an S corporation. In general, pursuant to the election, taxable income is taxed to the Stockholders and is not taxed at the corporate level. Therefore, no provisions or liabilities for federal or state income taxes have been included in these financial statements. Generally, the Company’s income tax returns are subject to examination by taxing authorities for up to three years after they are filed.

The Company has adopted the accounting guidance for uncertainty in income taxes using the provisions of FASB Accounting Standards Codification 740, Income Taxes. Using that guidance, tax positions initially need to be recognized in the financial statements when it is more-likely-than-not the positions will not be sustained upon examination by the tax authorities. Such tax positions initially and subsequently need to be measured as the largest amount of tax benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the tax authority, assuming full knowledge of the positions and relevant facts. It also provides guidance for derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. As of December 31, 2016 and 2015, the Company had no material uncertain tax positions that qualify for either recognition or disclosure in the financial statements and has incurred no interest or penalties related to unrecognized tax liabilities.

(g) Sales Tax - The Company contracts business with customers in a growing number of regions across the country with varying sales tax rules and regulations. The Company has internal control policies in place to correctly determine sales tax liabilities. However, due to the complexities of tax regulations, it is at least reasonably possible that sales tax liabilities could materialize.

(h) Management Estimates - The preparation of the 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, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(i) Reclassifications - Certain reclassifications have been made to the prior year amounts in order to conform to the current year financial statement presentation.

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(3) Billing and Collection Arrangements

The Company primarily utilizes its own internally developed and supported billing and collection system whereby customers establish an electronic account through prepayments to the Company. The accompanying balance sheets include approximately $1,153,000 and $1,138,000 in unearned revenues at December 31, 2016 and 2015, respectively. These totals, which if unused are refunded, represent the net amounts prepaid by customers for the completion of future calls.

The Company has partnered with third party providers to administer a debit system at inmate facilities where an inmate can transfer funds from their facility trust account to their own telephone account in order to make calls. Generally, unused amounts are returned to the inmate's account upon release from the facility. Net accounts receivable in the accompanying balance sheets include approximately $745,000 and $596,000 in amounts due from these third party providers at December 31, 2016 and 2015, respectively.

The Company also utilized the billing and collection services of various Local Exchange Carriers ("LECs"). The LECs billed and collected from the party that accepted calls under contracts with the Company. All remaining LEC contracts were terminated in 2015. Terms of certain LEC contracts allowed the LEC up to eighteen months to settle final amounts owed to the Company. As of December 31, 2016 and 2015, the LECs owed the Company approximately $125,000 and $133,000, respectively, which has been included in net accounts receivable and settlement reserve deposits in the accompanying balance sheets.

(4) Related Party Notes Receivable

The Company has notes receivable from trusts established by a Stockholder related to split-dollar life insurance policies. No interest has been charged on the outstanding balances. In 2013, the trusts notified the Company that the underlying life insurance policies were going to be surrendered and that the net cash surrender value would be inadequate to fully repay the amounts advanced by the Company in prior years. The Company only expects to receive the cash surrender value of the underlying insurance policies as repayment for the notes. As a result, the Company recorded a loss on notes receivable totaling approximately $61,000 and $55,000 in 2016 and 2015, respectively to reflect the changes in the cash surrender values.

(5) Impairment

The Company reviews all property and equipment for impairment when circumstances indicate the carrying amount of an asset may not be recoverable based on a variety of valuation techniques. During 2016, the Company recorded an impairment charge of $487,341 relating to certain information technology infrastructure software under development. As the Company has significantly modified future infrastructure development plans, it determined that certain software under development was fully impaired. The impairment charge is included in professional services in the accompanying 2016 statement of operations.

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(6) Financing

The Company has a working capital line of credit with a bank with maximum available borrowings of $1,000,000 and an equipment line of credit with maximum available borrowings of $2,000,000. The lines of credit incur interest on the outstanding balances at the one-month LIBOR (.77% at December 31, 2016) plus 2.5%. Interest only payments are due monthly through maturity in July 2017. The equipment line of credit is available to make equipment purchases and may be termed out under separate loan agreements and amortized over a period not to exceed five years.

The Company has an equipment loan with an outstanding principal balance of $901,201 and $1,190,000 at December 31, 2016 and 2015, respectively. The loan bears interest at the one-month LIBOR plus 2.5%. Payments of principal and interest totaling $26,760 are due monthly through December 2019 when all outstanding principal and interest is due.

The Company has an equipment loan with an outstanding principal balance of $57,910 and $193,391 at December 31, 2016 and 2015, respectively. The loan bears interest at 3.5%. Payments of principal and interest totaling $11,681 are due monthly through May 2017 when all outstanding principal and interest is due.

The Company had an equipment loan with an outstanding principal balance of $58,430 at December 31, 2015. The loan incurred interest at the one-month LIBOR plus 2.5%. Payments of principal totaling $14,583 plus applicable interest were due monthly through maturity in April 2016.

The approximate scheduled maturities of the equipment loans are as follows:

For the year ending December 31, 2017	$ 356,510
2018	307,500
2019	295,101
Total maturities	$ 959,111

All lines of credit and equipment loans are secured by all the property, equipment and other assets, certain cash accounts, the personal guarantee of a certain Stockholder, the assignment of all confinement facility contracts and the assignment of a certain life insurance policy on a certain Stockholder. The lines of credit and equipment loans also contain various covenants pertaining to the maintenance of certain financial ratios.

(7) Capitalized Lease

The Company has capital leases for equipment with a total cost of approximately $393,000. The leases are interest free and principal payments of approximately $2,639 and $9,054 are due monthly through January 2018 and February 2019, respectively. Depreciation on the leased equipment was approximately $86,100 and $29,100 in 2016 and 2015, respectively. Accumulated depreciation was approximately $115,200 and $29,100 at December 31, 2016 and 2015, respectively.

Future minimum lease payments under the capitalized lease and the present value of the net minimum lease payments are as follows:

For the year ending December 31,	2017	$ 130,800
	2018	108,000
	2019	9,011
Total minimum lease payments		247,811
Less amount representing interest		-
Present value of net minimum lease payments		$ 247,811

(8) Guarantee of Debt

The Company has fully guaranteed the debt of a Limited Liability Company ("LLC") owned by certain stockholders (Note 10) totaling approximately $912,000 and $1,037,000 at December 31, 2016 and 2015, respectively. The guarantee is not scheduled to expire. The Company would be required to provide a cash payment pursuant to the guarantee if the LLC were to default on the loan and it not be cured by the LLC or its owners. Because the estimated fair value of the LLC's collateral exceeds the amount of the debt obligation, significant losses are not anticipated. There is currently no recorded liability for potential losses under this guarantee, nor is there any liability for the Company's obligation to "stand ready" to fund such guarantee.

(9) Profit Sharing Plan

The Company has a retirement plan covering all employees who are at least 21 years of age and have at least ninety days of eligible service as defined in the plan. The retirement plan includes 401(k) and profit sharing features. Employees may contribute up to a maximum as allowed by the Internal Revenue Service, and the Company makes matching contributions equal to a discretionary percentage of the covered employees' contributions. Employees are fully vested in Company contributions after three years of eligible service. The Company made matching contributions of approximately $101,000 and $87,000 to the plan for 2016 and 2015, respectively and profit sharing contributions of $146,000 and $100,000 for 2016 and 2015, respectively.

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(10) Operating Leases and License Agreements

The Company leases its office and warehouse headquarters (approximately 49,000 square feet) from the LLC (Note 8). The lease requires monthly payments of approximately $34,800, expires in October 2018, and requires the Company to be responsible for all property taxes, insurance and operating expenses. Total rent paid to the LLC was approximately $417,000 for each of 2016 and 2015. The Company also has certain license agreements and leases various operations and office equipment, off-site storage and co-location facilities under separate lease agreements from third parties.

Future minimum payments are due as follows:

	Office & Warehouse	Other	Total
For the year ending December 31, 2017	$ 417,000	273,000	690,000
2018	347,700	3,500	351,200
Total future minimum payments due	$ 764,700	276,500	1,041,200

Total rental expense related to the operating leases for 2016 and 2015 was approximately $530,000 and $600,000, respectively.

(11) Florida Sales and Use Tax

During 2013, the Florida Department of Revenue ("Florida") completed an audit of the Company's activities in the state and assessed the Company approximately $385,000 for the period from June 1, 2006 through May 31, 2013. Including interest and penalties, the total amount charged by Florida was approximately $500,000.

In 2012, Florida completed a separate telecommunications tax audit of the Company which resulted in no additional tax due. The audit Florida completed in 2013 was for sales and use tax which the Company believed amounted to a tax on the same revenue that the Company paid with the telecommunications tax.

The Company filed a protest for the assessment on the premise that the sales and use tax did not apply to the Company based on the application of Florida tax laws. Although an actual final liability, if any, could not be determined at the time, the Company recorded an estimated liability of $200,000 as of December 31, 2015 related to this matter.

During 2016, Florida agreed with the Company's protest and rescinded the assessments levied. As such, the Company reversed the $200,000 estimated liability in 2016 and considers the matter closed.

(12) Subsequent Events

Management has evaluated subsequent events through April 17, 2017, the date which the financial statements were available to be issued.