

TUCOWS INC /PA/
Form 10-Q
May 08, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934**

For the quarterly period ended March 31, 2015

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE
ACT OF 1934**

For the transition period from to

Commission file number 1-32600

TUCOWS INC.

(Exact Name of Registrant as Specified in Its Charter)

Pennsylvania	23-2707366
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)

96 Mowat Avenue,

Toronto, Ontario M6K 3M1, Canada

(Address of Principal Executive Offices) (Zip Code)

(416) 535-0123

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T §232.405 of this chapter during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act): Yes No

As of May 6, 2015, there were 11,019,983 outstanding shares of common stock, no par value, of the registrant.

TUCOWS INC.

Form 10-Q Quarterly Report

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TRADEMARKS, TRADE NAMES AND SERVICE MARKS

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PART I.**FINANCIAL INFORMATION****Item 1. Consolidated Financial Statements****Tucows Inc.****Consolidated Balance Sheets****(Dollar amounts in U.S. dollars)****(unaudited)**

	March 31, 2015 (unaudited)	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	\$ 13,678,191	\$ 8,271,377
Accounts receivable, net of allowance for doubtful accounts of \$121,770 as of March 31, 2015 and \$125,766 as of December 31, 2014	7,119,785	6,789,685
Inventory	574,119	393,774
Prepaid expenses and deposits	5,085,514	3,697,292
Prepaid domain name registry and ancillary services fees, current portion	46,107,333	44,614,858
Other assets (note 5)	-	8,199,000
Deferred tax asset, current portion (note 9)	3,040,483	2,498,196
Income taxes recoverable	1,772	997
Total current assets	75,607,197	74,465,179
Prepaid domain name registry and ancillary services fees, long-term portion	11,735,134	11,764,765
Property and equipment	5,346,070	1,609,787
Deferred tax asset, long-term portion (note 9)	5,067,090	4,880,423
Intangible assets (note 7)	14,886,625	14,202,585
Goodwill (note 7)	21,055,143	18,873,127
Total assets	\$ 133,697,259	\$ 125,795,866

Liabilities and Stockholders' Equity

Current liabilities:		
Accounts payable	\$ 3,883,370	\$ 3,579,920

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Accrued liabilities	4,105,110	3,941,549
Customer deposits	4,325,284	4,461,727
Derivative instrument liability, (note 6)	2,139,268	1,115,805
Deferred rent, current portion	5,317	-
Loan payable (note 8)	3,500,000	-
Deferred revenue, current portion	57,630,217	55,495,566
Accreditation fees payable, current portion	519,432	466,201
Income taxes payable (note 9)	1,136,023	473,480
Total current liabilities	77,244,021	69,534,248
Deferred revenue, long-term portion	15,659,049	15,610,753
Accreditation fees payable, long-term portion	126,039	128,243
Deferred rent, long-term portion	85,069	92,878
Other liabilities (note 10)	1,545,832	-
Deferred tax liability, long-term portion (note 9)	5,032,177	4,787,351
Redeemable non-controlling interest (note 4)	3,000,000	-
Stockholders' equity (note 14)		
Preferred stock - no par value, 1,250,000 shares authorized; none issued and outstanding	-	-
Common stock - no par value, 250,000,000 shares authorized; 10,996,733 shares issued and outstanding as of March 31, 2015 and 11,329,732 shares issued and outstanding as of December 31, 2014	13,975,005	14,130,059
Additional paid-in capital	22,318,640	29,090,058
Deficit	(4,121,340)	(6,955,283)
Accumulated other comprehensive income (loss)	(1,167,233)	(622,441)
Total stockholders' equity	31,005,072	35,642,393
Total liabilities and stockholders' equity	\$ 133,697,259	\$ 125,795,866

Commitments and contingencies (note 13)

See accompanying notes to unaudited consolidated financial statements

Tucows Inc.**Consolidated Statements of Operations and Comprehensive Income****(Dollar amounts in U.S. dollars)****(unaudited)**

	Three months ended	
	March 31,	
	2015	2014
Net revenues (note 12)	\$40,467,833	\$34,402,394
Cost of revenues (note 12):		
Cost of revenues	26,821,374	24,316,639
Network expenses	1,222,096	1,143,644
Depreciation of property and equipment	199,642	182,974
Amortization of intangible assets (note 7)	3,924	-
Total cost of revenues	28,247,036	25,643,257
Gross profit	12,220,797	8,759,137
Expenses:		
Sales and marketing	3,799,175	4,021,774
Technical operations and development	1,114,195	1,089,898
General and administrative	1,815,188	1,767,800
Depreciation of property and equipment	59,262	56,304
Amortization of intangible assets (note 7)	53,215	219,030
Impairment of indefinite life intangible assets (note 7)	12,493	250,688
Loss on currency forward contracts (note 6)	956,858	551,371
Total expenses	7,810,386	7,956,865
Income from operations	4,410,411	802,272
Other income (expense):		
Interest expense, net	(24,775)	(73,833)
Total other income (expense)	(24,775)	(73,833)
Income before provision for income taxes	4,385,636	728,439
Provision for income taxes (note 9)	1,551,693	251,600
Net income	2,833,943	476,839

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Other comprehensive income (loss), net of tax		
Gain (loss) on hedging activities	(960,866)	(442,978)
Net amount reclassified to earnings	416,074	227,511
Other comprehensive income (loss) net of tax of \$319,878 and \$112,240 for the three months ended March 31, 2015 and March 31, 2014	(544,792)	(215,467)
Comprehensive income for the period	\$2,289,151	\$261,372
Basic earnings per common share (note 11)	\$0.25	\$0.04
Shares used in computing basic earnings per common share (note 11)	11,142,628	11,028,559
Diluted earnings per common share (note 11)	\$0.24	\$0.04
Shares used in computing diluted earnings per common share (note 11)	11,580,047	11,639,617

See accompanying notes to consolidated financial statements

Tucows Inc.**Consolidated Statements of Cash Flows****(Dollar amounts in U.S. dollars)****(unaudited)**

	Three months ended	
	March 31,	
	2015	2014
Cash provided by:		
Operating activities:		
Net income for the period	\$2,833,943	\$476,839
Items not involving cash:		
Depreciation of property and equipment	258,904	239,278
Amortization of intangible assets	57,139	219,030
Impairment of indefinite life intangible asset	12,493	250,688
Deferred income taxes recovery	(164,250)	(343,231)
Excess tax benefits from share-based compensation expense	-	(1,013,800)
Amortization of deferred rent	(2,492)	3,212
Disposal of domain names	6,328	1,622
Loss (gain) on change in the fair value of forward contracts	158,793	87,146
Stock-based compensation	125,048	100,977
Change in non-cash operating working capital:		
Accounts receivable	(168,585)	(1,262,921)
Inventory	(113,150)	(199,747)
Prepaid expenses and deposits	(1,299,778)	(366,836)
Prepaid domain name registry and ancillary services fees	(1,462,844)	(1,815,683)
Income taxes recoverable	661,768	(433,301)
Accounts payable	117,566	1,670,415
Accrued liabilities	(59,220)	(422,398)
Customer deposits	(136,443)	(29,129)
Deferred revenue	2,061,510	2,748,933
Accreditation fees payable	51,027	50,087
Net cash (used in) / provided by operating activities	2,937,757	(38,819)
Financing activities:		
Proceeds received on exercise of stock options	247,983	911,081
Excess tax benefits from share-based compensation expense	412,642	1,013,800
Repurchase of common stock	(7,712,145)	(82,286)
Proceeds received on loan payable	3,500,000	-
Repayment of loan payable	-	(616,667)
Net cash provided by / (used in) financing activities	(3,551,520)	1,225,928
Investing activities:		

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Additions to property and equipment	(191,762)	(68,745)
Gross proceeds from the waiver of rights to .online registry	6,619,832	-
Additional cost of acquisition of Ting Virginia, LLC., net of cash of \$21,423	(407,493)	-
Net cash provided by (used in) investing activities	6,020,577	(68,745)
Increase in cash and cash equivalents	5,406,814	1,118,364
Cash and cash equivalents, beginning of period	8,271,377	12,418,888
Cash and cash equivalents, end of period	\$ 13,678,191	\$ 13,537,252
Supplemental cash flow information:		
Interest paid	\$38,893	\$73,949
Income taxes paid, net	\$564,139	\$669,624
Supplementary disclosure of non-cash investing and financing activities:		
Property and equipment acquired during the period not yet paid for	\$66,798	\$285,821

See accompanying notes to unaudited consolidated financial statements

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

1. ORGANIZATION OF THE COMPANY:

Tucows Inc., a Pennsylvania corporation (referred to throughout this report as the “Company”, “Tucows”, “we”, “us” or through similar expressions), together with our consolidated subsidiaries, is a global distributor of Internet services, including domain name registration, security and identity products through digital certificates, email and mobile telephony and fixed Internet access services. The Company’s Internet Services are distributed through its global Internet-based distribution network of Internet Service Providers, web hosting companies and other providers of Internet services to end-users

We were incorporated under the laws of the Commonwealth of Pennsylvania in November 1992 under the name Infonautics, Inc. In August 2001, we completed our acquisition of Tucows Inc., a Delaware corporation, and we changed our name from Infonautics, Inc. to Tucows Inc. Our principal executive office is located in Toronto, Ontario and we have other offices in the Netherlands, Germany and the United States. Our common stock is listed on NASDAQ under the symbol “TCX” and on the Toronto Stock Exchange under the symbol “TC”.

2. BASIS OF PRESENTATION:

The accompanying unaudited interim consolidated balance sheets, and the related consolidated statements of operations and comprehensive income and cash flows reflect all adjustments, consisting of normal recurring adjustments, that are, in the opinion of management, necessary for a fair presentation of the financial position of Tucows and its subsidiaries as at March 31, 2015 and the results of operations and cash flows for the interim periods ended March 31, 2015 and 2014. The results of operations presented in this Quarterly Report on Form 10-Q are not necessarily indicative of the results of operations that may be expected for future periods.

The accompanying unaudited interim consolidated financial statements have been prepared by Tucows in accordance with the rules and regulations of the Securities and Exchange Commission (the “SEC”). Certain information and footnote disclosure normally included in the Company's annual audited consolidated financial statements and accompanying notes have been condensed or omitted. These interim consolidated financial statements and accompanying notes follow the same accounting policies and methods of application used in the annual financial statements and should be read in conjunction with the Company's audited consolidated financial statements and notes thereto for the year ended December 31, 2014 included in Tucows' 2014 Annual Report on Form 10-K filed with the SEC on March 11, 2015.

There have been no material changes to our significant accounting policies during the three months ended March 31, 2015 as compared to the significant accounting policies described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2014.

For purposes of clarification, significant accounting policies regarding revenue recognition and derivative financial instruments are included below:

(a) Revenue recognition

The Company's revenues are derived from domain name registration fees on both a wholesale and retail basis, the sale of domain names, the provisioning of other Internet services and advertising and other revenue. Amounts received in advance of meeting the revenue recognition criteria described below are recorded as deferred revenue.

The Company earns registration fees in connection with each new, renewed and transferred-in registration and from providing provisioning of other Internet services to resellers and registrars on a monthly basis. Service has been provided in connection with registration fees once the Company has confirmed that the requested domain name has been appropriately recorded in the registry under contractual performance standards.

Domain names are generally purchased for terms of one to ten years. Registration fees charged for domain name registration and provisioning services are recognized on a straight-line basis over the life of the contracted term. Other Internet services that are provisioned for annual periods or longer, are recognized on a straight-line basis over the life of the contracted term. Other Internet services that are provisioned on a monthly basis are recognized as services are provided.

For arrangements with multiple deliverables, the Company allocates revenue to each deliverable if the delivered item(s) has value to the customer on a standalone basis and, if the arrangement includes a general right of return relative to the delivered item, delivery or performance of the undelivered item(s) is considered probable and substantially in the control of the Company. The fair value of the selling price for a deliverable is determined using a hierarchy of (1) Company specific objective and reliable evidence, then (2) third-party evidence, then (3) best estimate of selling price. The Company allocates any arrangement fee to each of the elements based on their relative selling prices.

Revenue generated from the sale of domain names, earned from transferring the rights to domain names under the Company's control, are recognized once the rights have been transferred and payment has been received in full.

The Company derives revenues from the provisioning of mobile phone and fixed Internet access services through its Ting website. These revenues are recognized once services have been provided. Revenues for wireless services are billed based on the actual amount of monthly services utilized by each customer during their billing cycle on a postpaid basis. The Company's billing cycle for each customer is computed based on the customer's activation date. As a result, the Company estimates the amount of revenues earned but not billed from the end of each billing cycle to the end of each reporting period. In addition, revenues associated with the sale of wireless devices and accessories to subscribers is recognized when title and risk of loss is transferred to the subscriber and shipment has occurred. Incentive marketing credits given to customers are recorded as a reduction of revenue.

The Company also generates advertising and other revenue through its online libraries of shareware, freeware and online services presented on its website. Advertising revenue includes revenue derived from cost-per action advertising links we display on third party websites who provide syndicated pay-per-click advertising on OpenSRS Domain Expiry Stream domains and the Company's Portfolio Domains. In addition, the Company uses third party partners to derive pay-per-click advertising on the Tucow.com website. Advertising revenue is recognized on a monthly basis based on the number of cost-per-action services that were provided in the month.

In those cases where payment is not received at the time of sale, additional conditions for recognition of revenue are that the collection of the related accounts receivable is reasonably assured and the Company has no further performance obligations. The Company records costs that reflect expected refunds, rebates and credit card charge-backs as a reduction of revenues at the time of the sale based on historical experiences and current expectations.

The Company establishes provisions for possible uncollectible accounts receivable and other contingent liabilities which may arise in the normal course of business. Historically, credit losses have been within the Company's expectations and the provisions the Company has established have been appropriate. However, the Company has, on occasion, experienced issues which have led to accounts receivable not being fully collected. Should these issues occur more frequently, additional provisions may be required.

(b) Property and equipment

Property and equipment are stated at cost, net of accumulated depreciation. Depreciation is provided on a straight-line basis so as to depreciate the cost of depreciable assets over their estimated useful lives at the following rates:

Asset	Rate
Computer equipment	30 %
Computer software	100 %
Furniture and equipment	20 %
Vehicles	20 %
Fiber network (years)	15
Customer equipment and installations (years)	3
Leasehold improvements	Over term of lease

The Company reviews the carrying values of its property and equipment for potential impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If the estimated undiscounted future cash flows expected to result from the use of the group of assets and its eventual disposition is less than its carrying amount, it is considered to be impaired. The amount of the impairment loss recognized is measured as the amount by which the carrying value of the asset exceeds the fair value of the asset, with fair value being determined based upon discounted cash flows or appraised values, depending on the nature of the assets.

Additions to the fiber network are recorded at cost, including all material, labour, vehicle and installation and construction costs and certain indirect costs associated with the construction of cable transmission and distribution facilities. While the Company's capitalization is based on specific activities, once capitalized, costs are tracked by fixed asset category at the fiber network level and not on a specific asset basis. For assets that are retired, the estimated historical cost and related accumulated depreciation is removed.

Costs associated with initial customer installation include materials, labour, vehicle and installation and construction costs and certain indirect costs. Indirect costs are associated with the activities of the Company's personnel who assist in connecting and activating the new service and consist of compensation and other costs associated with these support functions.

The costs of disconnecting service at a customer's dwelling or reconnecting service to a previously installed dwelling are charged to operating expense in the period incurred. Costs for repairs and maintenance are charged to operating expense as incurred, while plant and equipment replacement and betterments, including replacement of cable drops from pole to the dwelling, are capitalized.

(c) Derivative Financial Instruments

During the three months ended March 31, 2015 and the year ended December 31, 2014 ("Fiscal 2014"), we used derivative financial instruments to manage foreign currency exchange risk. We account for these instruments in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 815, "Derivatives and Hedging" ("Topic 815"), which requires that every derivative instrument be recorded on the balance sheet as either an asset or liability measured at its fair value as of the reporting date. Topic 815 also requires that changes in our derivative financial instruments' fair values be recognized in earnings, unless specific hedge accounting and documentation criteria are met (i.e. the instruments are accounted for as hedges). We recorded the effective portions of the gain or loss on derivative financial instruments that were designated as cash flow hedges in accumulated other comprehensive income in our accompanying Consolidated Balance Sheets. Any ineffective or excluded portion of a designated cash flow hedge, if applicable, is recognized in net income.

For certain contracts, the Company has not complied with the documentation standards required for its forward foreign exchange contracts to be accounted for as hedges and has, therefore, accounted for such forward foreign exchange contracts at their fair values with the changes in fair value recorded in net income.

The fair value of the forward exchange contracts are determined using an estimated credit adjusted mark-to-market valuation which takes into consideration the Company's and the counterparty's credit risk. The valuation technique used to measure the fair values of the derivative instruments is a discounted cash flow technique, with all significant inputs derived from or corroborated by observable market data, as no quoted market prices exist for the derivative instruments. Our discounted cash flow techniques use observable market inputs, such as foreign currency spot and forward rates.

3. NEW ACCOUNTING POLICIES:

Recent Accounting Pronouncements Adopted

In May 2014, the FASB issued Accounting Standards Update ("ASU") No. 2014-09, *Revenue from Contracts with Customers* ("ASU 2014-09"), which is a comprehensive revenue recognition standard that will supersede nearly all existing revenue recognition guidance under U.S. GAAP. The new standard provides a single principles-based, five-step model to be applied to all contracts with customers, which steps are to (1) identify the contract(s) with the customer, (2) identify the performance obligations in the contract, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations in the contract and (5) recognize revenue when each performance obligation is satisfied. More specifically, revenue will be recognized when promised goods or services are transferred to the customer in an amount that reflects the consideration expected in exchange for those goods or services. ASU 2014-09 will be effective, reflecting the one-year proposed deferral, for interim and annual periods beginning after December 15, 2017 (January 1, 2018 for the Company). Early adoption of the standard is permitted but not before the original effective date. Companies can transition to the standard either retrospectively or as a cumulative-effect adjustment as of the date of adoption. The Company is currently in the process of evaluating the impact that the adoption of ASU 2014-09 will have on its consolidated financial statements and the selected method of transition to the new standard.

In April 2015, the FASB issued ASU No. 2015-05, *Customer's Accounting for Fees Paid in a Cloud Computing Arrangement* ("ASU 2015-05"), which provides guidance in determining whether fees for purchasing cloud computing services (or hosted software solutions) are considered internal-use software or should be considered a service contract. The cloud computing agreement that includes a software license should be accounted for in the same manner as internal-use software if customer has contractual right to take possession of the software during the hosting period without significant penalty and it is feasible to either run the software on customer's hardware or contract with another vendor to host the software. Arrangements that don't meet the requirements for internal-use software should be accounted for as a service contract. ASU 2015-05 will be effective for interim and annual periods beginning after December 15, 2015 (January 1, 2016 for the Company). Early adoption of the standard is permitted. The Company is currently in the process of evaluating the impact that the adoption of ASU 2015-05 will have on its consolidated financial statements.

4. Acquisitions and Divestitures:

Acquisitions

On February 27, 2015, Ting Fiber, Inc., one of our wholly owned subsidiaries, acquired a 70% ownership interest in the newly formed Ting Virginia, LLC and its acquired subsidiaries, Blue Ridge Websoft, LLC (doing business as Blue Ridge InternetWorks), Fiber Roads, LLC and Navigator Network Services, LLC (the “BRI Group”) for a consideration of approximately \$3.6 million, subject to additional customary adjustments as anticipated in the purchase agreement, primarily related to estimated working capital levels at closing. The purchase price was satisfied through our releasing \$3.1 million from the escrow accounts established during Fiscal 2014 and an additional payment of \$0.4 million made at closing. Ting Virginia, LLC is an independent Internet service provider in Charlottesville, Virginia, doing business primarily as Blue Ridge InternetWorks. The BRI Group provides high speed internet access, Internet hosting and network consulting services to over 3,000 customers in central Virginia. The purchase price was primarily satisfied through an advance under our 2012 DLR Loan facility.

Ting Fiber Inc. and the selling shareholders (the “Minority Shareholders”) also agreed to certain put and call options with regard to the remaining 30% interest in Ting Virginia, LLC retained by the Minority Shareholders. On the second anniversary of the closing date, Ting Fiber, Inc. may exercise a call option to purchase an additional 20% ownership interest in Ting Virginia, LLC. Contingent upon the exercise of the call option by Ting Fiber, Inc. the Minority Shareholders may exercise a put option within 7 days following the exercise of the call option by Ting Fiber, Inc., to sell their remaining 10% ownership interest in Ting Virginia LLC. The consideration to be exchanged for the shares acquired or sold under the options shall be \$100,000 per percentage point of the equity interest acquired.

In addition, on the fourth anniversary of the closing date, the Minority Shareholders may exercise a put option under which the Ting Fiber Inc. shall be irrevocably obligated to purchase the Minority Shareholders’ remaining interest for \$120,000 per percentage point of the equity interest acquired for a total of \$3,600,000.

The Company has determined that the put options described above are embedded within the non-controlling interest shares that are subject to the put options. The redemption feature requires classification of the Minority Shareholders’ Interest in the Consolidated Balance Sheets outside of equity under the caption “Redeemable non-controlling interest”. The present value of the liability at the acquisition date is \$3,000,000.

The preliminary purchase consideration is comprised as follows:

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Cash	\$3,135,140
Assumption of debt	418,775
Redeemable non-controlling interest	3,000,000
	\$6,553,915

The following table represents the purchase price allocation based on the estimated fair values of the assets

Current assets (including cash of \$21,423)	\$338,577
Current liabilities	(529,702)

Property and equipment, including:	
Fiber network	3,456,024
Computer equipment	200,000
Furniture and equipment	5,000
Vehicles	92,000
Leasehold improvements	50,000

Intangible assets, including:	
Network rights	692,000
Customer relationships	68,000

Goodwill	2,182,016
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Net assets acquired	\$6,553,915
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The goodwill recorded on the acquisition is expected to be deductible for tax purposes.

The fair value of current assets acquired includes accounts receivable with a fair value of \$0.2 million. All accounts receivable acquired at acquisition are expected to be collectable.

The acquisition had no significant impact on revenues and net earnings for the three months ended March 31, 2015. There was also no significant impact on the Company's revenues and net income on a pro forma basis for all periods presented.

The Company acquired new classes of assets in this acquisition, namely fiber network and vehicles. The Company has accordingly, in connection with its depreciation policies, added additional disclosure in note 2 (b) above.

5. Other assets:

Other assets are comprised of the following:

	Year ended March 31, 2015	Year ended December 31, 2014
Amounts in escrow advanced to acquire a controlling ownership interest in Ting Virginia, LLC (see note 4)	\$	— \$3,125,000
Amounts advanced to the joint venture with Radix FZC and NameCheap Inc. which was terminated in February 2015 (note 10)		— 5,074,000
	\$	— \$8,199,000

6. Derivative instruments and hedging activities:*Foreign currency forward contracts*

In October 2012, the Company entered into a hedging program with a Canadian chartered bank to limit the potential foreign exchange fluctuations incurred on its future cash flows related to a portion of payroll, rent and payments to Canadian domain name registry suppliers that are denominated in Canadian dollars and are expected to be paid by its Canadian operating subsidiary. As part of its risk management strategy, the Company uses derivative instruments to hedge a portion of the foreign exchange risk associated with these costs. The Company does not use these forward contracts for trading or speculative purposes. These forward contracts typically mature between one and eighteen months.

The Company has designated these transactions as cash flow hedges of forecasted transactions under ASC Topic 815. As the critical terms of the hedging instrument, and of the entire hedged forecasted transaction, are the same, in accordance with ASC Topic 815, the Company has been able to conclude that changes in fair value or cash flows attributable to the risk of being hedged are expected to completely offset at inception and on an ongoing basis. Accordingly, unrealized gains or losses on the effective portion of these contracts have been included within other comprehensive income. The fair value of the contracts, as of March 31, 2015, is recorded as derivative instrument liabilities.

As of March 31, 2015, the notional amount of forward contracts that the Company held to sell U.S. dollars in exchange for Canadian dollars was \$19.5 million, of which \$16.5 million met the requirements of ASC Topic 815 and were designated as hedges (March 31, 2014 - \$20.1 million of which \$15.6 million were designated as hedges).

Fair value of derivative instruments and effect of derivative instruments on financial performance

The effect of these derivative instruments on our consolidated financial statements as of, and for the three months ended March 31, 2015, were as follows (amounts presented do not include any income tax effects).

Fair value of derivative instruments in the consolidated balance sheets

Derivatives	Balance Sheet Location	As of	As of
		March 31, 2015	December 31, 2014
		Fair Value	Fair Value
		Asset	Asset
		(Liability)	(Liability)
Foreign currency forward contracts not designated as cash flow hedges	Derivative instruments	\$(327,922)	\$(169,129)
Foreign currency forward contracts designated as cash flow hedges	Derivative instruments	\$(1,811,346)	\$(946,676)
Total foreign currency forward contracts	Derivative instruments	\$(2,139,268)	\$(1,115,805)

Movement in Accumulated Other Comprehensive Income ("AOCI") balance for the three months ended March 31, 2015:

	Gains and losses on cash flow hedges	Tax impact	Total AOCI
Opening AOCI balance – December 31, 2014	\$(946,676)	\$324,235	\$(622,441)
Other comprehensive income (loss) before reclassifications	(1,510,346)	549,480	(960,866)
Amount reclassified from accumulated other comprehensive income	645,676	(229,602)	416,074
Other comprehensive income (loss) for the three months ended March 31, 2015	(864,670)	319,878	(544,792)
Ending AOCI balance – March 31, 2015	\$(1,811,346)	\$644,113	\$(1,167,233)

Effects of derivative instruments on income and other comprehensive income (OCI) for the three months ended March 31, 2015 and March 31, 2014 are as follows:

Derivatives in Cash Flow	Amount of Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)	Location of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Amount of Gain or (Loss) Reclassified from Accumulated OCI into Income (Effective Portion)	Location of Gain or (Loss) Recognized in Income on Derivative (ineffective Portion and Amount Excluded from Effectiveness Testing)	Amount of Gain or (Loss) Recognized in Income on Derivative (ineffective Portion and Amount Excluded from Effectiveness Testing)
Hedging Relationship					
Foreign currency forward contracts for the three months ended March 31, 2015		Operating expenses	\$ (301,590)		
	\$ (544,792)	Cost of revenues	(114,484)	Operating expenses	\$ (15,419)

		Operating expenses	\$ (168,620)	
Foreign currency forward contracts for the three months ended March 31, 2014	\$ (215,467)	Cost of revenues	(58,891)	Operating expenses \$ —

In addition to the above, for those foreign currency forward contracts not designated as hedges, the Company has recorded a loss of \$0.1 million upon settlement and a loss of \$0.2 million for the change in fair value of outstanding contracts for the three months ended March 31, 2015, in the consolidated statement of operations and comprehensive income. The Company has recorded a loss of \$0.1 million upon settlement and a loss of \$0.1 million for the change in fair value of outstanding contracts for the three months ended March 31, 2014, in the consolidated statement of operations and comprehensive income.

7. Goodwill and Other Intangible Assets:

Goodwill

Goodwill represents the excess of purchase price over the fair value of tangible or identifiable intangible assets acquired and liabilities assumed in our acquisitions.

Goodwill consists of the following:

	Boardtown Corporation	Hosted Messaging Assets of Critical Path	Innerwise Inc.	Mailbank.com Inc.	EPAG Domainservice GmbH	BRI Group	Total
Balances, December 31, 2014	\$ 2,044,847	\$ 4,072,297	\$ 5,801,040	\$ 6,072,623	\$ 882,320	\$ -	\$ 18,873,127
Acquisition of BRI Group, February 2015	-	-	-	-	-	2,182,016	2,182,016
Balances, March 31, 2015	\$ 2,044,847	\$ 4,072,297	\$ 5,801,040	\$ 6,072,623	\$ 882,320	\$ 2,182,016	\$ 21,055,143

The Company's goodwill relates predominantly to its Domain Services operating segment.

On February 27, 2015, Ting Fiber, Inc., one of our wholly owned subsidiaries, acquired a 70% ownership interest in the BRI Group. Goodwill is not amortized, but is subject to an annual impairment test.

Other Intangible Assets:

Intangible assets consist of network rights, brand, customer relationships, surname domain names, non-competition agreements and our portfolio of domain names. As reflected in the table below, these balances are being amortized on a straight-line basis over the life of the intangible assets, except for the surname domain names and portfolio domain names, which have been determined to have an indefinite life and which are tested annually for impairment.

A summary of acquired intangible assets for the three months ended March 31, 2015 is as follows:

	Brand	Customer relationships	Network rights	Surname domain names	Direct navigation domain names	
	7 years	4 - 7 years	15 years	indefinite life	indefinite life	Total
Net book value, December 31, 2014	\$ 110,510	\$ 625,220	\$ -	\$ 11,525,624	\$ 1,941,231	\$ 14,202,585
Acquisition of BRI Group, February 2015	-	68,000	692,000	-	-	760,000
Sales of domain names	-	-	-	(1,623)	(4,705)	(6,328)
Impairment of domain names	-	-	-	(7,788)	(4,705)	(12,493)
Amortization expense	(7,710)	(45,505)	(3,924)	-	-	(57,139)
Net book value, March 31, 2015	\$ 102,800	\$ 647,715	\$ 688,076	\$ 11,516,213	\$ 1,931,821	\$ 14,886,625

As of March 31, 2015, the accumulated amortization for the definite life intangibles was \$5.7 million.

With regard to indefinite life intangible assets, as part of our normal renewal process we assessed that certain domain names that were acquired in the June 2006 acquisition of Mailbank.com Inc. that were up for renewal should not be renewed. Accordingly, for the three months ended March 31, 2015, domain names, with a book value of \$12,493 (three months ended March 31, 2014 - \$0.3 million), were not renewed and were recorded as an impairment of indefinite life intangible assets.

8. LOAN PAYABLE:

The Company has credit agreements (collectively the “Amended Credit Facility”) with the Bank of Montreal (the “Bank” or “BMO”) that were amended on November 19, 2012, and which provide it with access to two revolving demand loan facilities (the “2012 Demand Loan Facilities”), a treasury risk management facility and an operating demand loan.

Two Revolving Demand Loan Facilities.

The 2012 Demand Loan Facilities are governed by the terms of the Offer Letter, dated as of November 19, 2012, by and between the Company and the Bank and filed with the SEC on November 21, 2012.

Under the terms of the Amended Credit Facility, our prior demand loan facilities have been amended to provide an aggregate of \$14 million in funds available through the 2012 Demand Loan Facilities, which consist of a demand loan revolving facility (the “2012 DLR Loan”) and a demand loan revolving reducing facility (the “2012 DLRR Loan”). The 2012 DLR Loan accrues interest at the Bank’s U.S. Base Rate plus 1.25%. The Company may elect to pay interest on the 2012 DLRR Loan either at the Bank’s U.S. Base Rate plus 1.25% or LIBOR plus 2.50%. Aggregate advances under the 2012 Demand Loan Facilities may not exceed \$14 million and no more than \$2 million of such advances may be used to finance repurchases of Company common stock. The 2012 Demand Loan Facilities are subject to an undrawn aggregate standby fee of 0.20% following the first draw, which such fee is payable quarterly in arrears.

Repayment of advances under the 2012 DLR Loan consist of interest only payments made monthly in arrears and prepayment is permitted without penalty. The outstanding balance under the 2012 DLR Loan as of December 31st of each year is to be fully repaid within 30 days of December 31st through an equivalent advance made under the 2012 DLRR Loan. Advances under the 2012 DLRR Loan will be made annually and solely for such purpose. Each advance under the 2012 DLRR Loan is to be repaid in equal monthly principal payments plus interest, over a period of four years from the date of such advance.

On January 7, 2015, the Company successfully concluded a modified “Dutch auction tender offer”, which was funded from available cash. Under the terms of the offer, the Company repurchased an aggregate of 193,907 shares of its common stock at a purchase price of \$18.50 per share, for a total of \$3,587,280, excluding transaction costs of approximately \$70,000. At March 31, 2015, the outstanding balance under the 2012 DLR Loan was \$3.5 million (December 31, 2014 - Nil).

During the three months ended March 31, 2015 no amounts were drawn down on the 2012 DLRR Loan. At March 31, 2015, the 2012 DLRR Loan was fully repaid. This financing arrangement remain available to fund future operations of the Company, with no set expiry date.

Treasury Risk Management Facility

The Amended Credit Facility also provides for a \$3.5 million settlement risk line to assist the Company with hedging Canadian dollar exposure through foreign exchange forward contracts and/or currency options. Under the terms of the Amended Credit Facility, the Company may enter into such agreements at market rates with terms not to exceed 18 months. As of March 31, 2015, the Company held contracts in the amount of \$19.5 million to trade U.S. dollars in exchange for Canadian dollars.

Operating Demand Loan

The Amended Credit Facility also provides the Company with a \$1.0 million operating demand loan facility to assist in meeting its operational needs (the “Operating Demand Loan”). The Operating Demand Loan accrues interest at the Bank’s U.S. Base Rate plus 1.25%. Interest is payable monthly in arrears with any borrowing under the Operating Demand Loan fluctuating widely with periodic clean-up, at a minimum on an annual basis. The Company has also agreed to pay to the Bank a monthly monitoring fee of US\$500 with respect to this loan. The Operating Demand Loan is payable on demand at any time, at the sole discretion of the Bank, with or without cause, and the Bank may terminate the Operating Demand Loan at any time. As of March 31, 2015, the Company had no amounts outstanding under its Operating Demand Loan.

General Terms

The Company’s Amended Credit Facility contains customary representations and warranties, affirmative and negative covenants, and events of default. The Company’s obligations under the Amended Credit Facility are guaranteed and secured by a security interest in substantially all of its assets. The Amended Credit Facility also requires that the

Company comply with certain customary non-financial covenants and restrictions. In addition, the Company has agreed to comply with the following financial covenants at all times, which are to be calculated on a rolling four quarter basis: (i) Maximum Total Funded Debt to EBITDA of 2.00:1; and (ii) Minimum Fixed Charge Coverage of 1.20:1. Further, its Maximum Annual Capital Expenditures cannot exceed \$3.6 million per year, which limit will be reviewed on an annual basis. As at and for the period ended, March 31, 2015, the Company was in compliance with these covenants. As at and for the period ended, March 31, 2014, the Company was in compliance with these covenants.

9. INCOME TAXES

For the three months ended March 31, 2015, the Company recorded a provision for income taxes of \$1.6 million on income before income taxes of \$4.4 million, using an estimated effective tax rate for the fiscal year ending December 31, 2015 adjusted for certain minimum state taxes. Comparatively, for the three months ended March 31, 2014, the Company recorded a provision for income taxes of \$0.3 million on income before taxes of \$0.7 million, using an estimated effective tax rate for its fiscal year ending December 31, 2014.

In assessing the realizability of deferred tax assets, the Company considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the years in which those temporary differences become deductible. The Company considers projected future taxable income, uncertainties related to the industry in which we operate, and tax planning strategies in making this assessment.

The Company follows the provisions of FASB ASC Topic 740, Income Taxes to account for income tax exposures. The application of this interpretation requires a two-step process that separates recognition of uncertain tax benefits from measurement thereof.

The Company had approximately \$0.1 million of total gross unrecognized tax benefit as of March 31, 2015 and as of December 31, 2014, which if recognized would favorably affect its income tax rate in future periods. The unrecognized tax benefit relates primarily to prior year Pennsylvania state franchise taxes. The Company recognizes accrued interest and penalties related to income taxes in income tax expense. The Company did not have significant interest and penalties accrued at March 31, 2015 and December 31, 2014, respectively.

10. OTHER LIABILITIES:

In February 2015, the Company waived its rights under the formerly proposed joint venture to operate the .online registry and instead entered into a Joint Marketing agreement with its venture partners under which its original capital contributions have been returned and a set of go-forward marketing arrangements have been created instead. These marketing arrangements have resulted in the Company receiving a gain of \$1.5 million, which will be recognized evenly over the three-year term of the marketing agreement once .online is generally available.

11. BASIC AND DILUTED EARNINGS PER COMMON SHARE:

Basic earnings per common share has been calculated by dividing net income for the period by the weighted average number of common shares outstanding during each period. Diluted earnings per share has been calculated by dividing net income for the period by the weighted average number of common shares and potentially dilutive common shares outstanding during the period. In computing diluted earnings per share, the treasury stock method is used to determine the number of shares assumed to be purchased from the conversion of common shares equivalents or the proceeds of option exercises.

The following table is a summary of the basic and diluted earnings per common share:

	Three months ended	Three months ended
	March 31, 2015	March 31, 2014
Numerator for basic and diluted earnings per common share:		
Net income for the period	\$2,833,943	\$476,839
Denominator for basic and diluted earnings per common share:		
Basic weighted average number of common shares outstanding	11,142,628	11,028,559

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Effect of outstanding stock options	437,419	611,058
Diluted weighted average number of shares outstanding	11,580,047	11,639,617
Basic earnings per common share	\$0.25	\$0.04
Diluted earnings per common share	\$0.24	\$0.04

For the three months ended March 31, 2015, outstanding options to purchase 116,600 common shares were not included in the computation of diluted income per common share because all such options had exercise prices greater than the average market price of the common shares.

During the three months ended March 31, 2015, 193,907 common shares were repurchased and cancelled under the terms of a modified Dutch auction tender offer announced in December 2014.

During the three months ended March 31, 2015, 214,089 common shares were repurchased and cancelled under the terms of our stock repurchase program announced in February 2015.

During the three months ended March 31, 2014, 6,092 common shares were repurchased and cancelled under the terms of our stock repurchase program announced in March 2014.

The computation of earnings per share and diluted earnings per share for the three months ended March 31, 2015 and 2014 include reductions in the number of shares outstanding due to these repurchases.

12. SEGMENT REPORTING:

(a) We are organized and managed based on two segments, which are differentiated primarily by their services, the markets they serve and the regulatory environments in which they operate. The two segments are Domain Services and Network Access Services and are described as follows:

1. Domain Services – This segment includes wholesale and retail domain name registration services, value added services and portfolio services. The Company primarily earns revenues from the registration fees charged to resellers in connection with new, renewed and transferred domain name registrations; the sale of retail Internet domain name registration and email services to individuals and small businesses; and by making its portfolio of domain names available for sale or lease. Domain Services revenues are attributed to the country in which the contract originates, primarily Canada.

2. Network Access Services - This segment derives revenue from the sale of retail mobile phones and services to individuals and small businesses through the Ting website, as well as provides high speed Internet access, Internet hosting and network consulting to customers in Central Virginia through its acquisition of a 70% share in Ting Virginia, LLC. Revenues are generated in the United States.

The Chief Executive Officer is the chief operating decision maker and regularly reviews the operations and performance by segment. The chief operating decision maker reviews gross margin as a key measure of performance for each segment and to make decisions about the allocation of resources. Sales and marketing expenses, technical operations and development expenses, general and administrative expenses, depreciation of property and equipment, loss on disposition of property and equipment, amortization of intangibles, loss (gain) on currency forward contracts, other income (expense), and provision for income taxes, are organized along functional lines and are not included in the measurement of segment profitability. Total assets and total liabilities are centrally managed and are not reviewed at the segment level by the chief operating decision maker.

Information by reportable segments, which is regularly reported to the chief operating decision maker is as follows:

	Domain Name Services	Network Access Services	Consolidated Totals
Three months ended March 31, 2015			
Net Revenues	\$27,540,819	\$12,927,014	\$40,467,833
Cost of Revenues	19,476,217	7,345,157	26,821,374
Gross Profit before network expenses	8,064,602	5,581,857	13,646,459

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Network expenses	1,425,662
Gross Profit	12,220,797

Expenses:

Sales and marketing	3,799,175
Technical operations and development	1,114,195
General and administrative	1,815,188
Depreciation of property and equipment	59,262
Amortization of intangibles	53,215
Impairment of indefinite life intangible assets	12,493
Loss on currency forward contracts	956,858
Income from operations	4,410,411
Other expenses, net	24,775
Income before provision for income taxes	\$4,385,636

Three months ended March 31, 2014	Domain	Network	Consolidated
	Name	Access	
	Services	Services	Totals
Net Revenues	\$27,690,262	\$6,712,132	\$34,402,394
Cost of Revenues	20,035,208	4,281,431	24,316,639
Gross Profit before network expenses	7,655,054	2,430,701	10,085,755
Network expenses			1,326,618
Gross Profit			8,759,137
Expenses:			
Sales and marketing			4,021,774
Technical operations and development			1,089,898
General and administrative			1,767,800
Depreciation of property and equipment			56,304
Amortization of intangibles			219,030
Impairment of indefinite life intangible assets			250,688
Loss on currency forward contracts			551,371
Income from operations			802,272
Other expenses, net			73,833
Income before provision for income taxes			\$728,439

(b) The following is a summary of the Company's revenue earned from each significant revenue stream:

	Three months ended	
	March 31,	
	2015	2014
<u>Domain Services:</u>		
Wholesale		
Domain Services	\$21,175,131	\$21,648,954
Value Added Services	2,241,998	2,603,605
Total Wholesale	23,417,129	24,252,559
Retail	2,875,728	2,384,063
Portfolio	1,247,962	1,053,640
Total Domain Services	27,540,819	27,690,262
<u>Network Access Services:</u>		
Ting	12,927,014	6,712,132
Total Network Access Services	12,927,014	6,712,132
	\$40,467,833	\$34,402,394

During the three months ended March 31, 2015 and 2014, no customer accounted for more than 10% of total revenue. As at March 31, 2015 and 2014, no customer accounted for more than 10% of accounts receivable.

(c) The following is a summary of the Company's cost of revenues from each significant revenue stream:

	Three months ended	
	March 31,	
	2015	2014
<u>Domain Services:</u>		
Wholesale		
Domain Services	\$17,548,027	\$18,235,215
Value Added Services	536,132	540,722
Total Wholesale	18,084,159	18,775,937
Retail	1,220,500	1,015,416
Portfolio	171,558	243,855

Total Domain Services	19,476,217	20,035,208
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Network Access Services:

Ting	7,345,157	4,281,431
Total Network Access Services	7,345,157	4,281,431

Network Expenses:

Network, other costs	1,222,096	1,143,644
Network, depreciation and amortization costs	203,566	182,974
Total Network Expenses	1,425,662	1,326,618

	\$28,247,036	\$25,643,257
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(d) The following is a summary of the Company's property and equipment by geographic region:

	March 31, 2015	December 31, 2014
Canada	\$1,122,910	\$1,131,883
United States	4,145,540	379,891
Germany	77,620	98,013
	\$5,346,070	\$1,609,787

(e) The following is a summary of the Company's amortizable intangible assets by geographic region:

	March 31, 2015	December 31, 2014
United States	\$754,191	\$—
Germany	684,400	735,730
	\$1,438,591	\$735,730

(f) The following is a summary of the Company's deferred tax asset, net of valuation allowance, by geographic region:

	March 31, 2015	December 31, 2014
Canada	\$8,107,573	\$7,378,619
	\$8,107,573	\$7,378,619

(g) Valuation and qualifying accounts:

	Balance at beginning period	Charged to (recovered) costs and expenses	Write-offs during period	Balance at end of period
Allowance for doubtful accounts, excluding provision for credit notes				
Three months ended March 31, 2015	\$ 125,766	\$ 3,996	\$ —	\$ 121,770
Year ended December 31, 2014	\$ 91,226	\$ (34,540)	\$ —	\$ 125,766

13. COMMITMENTS AND CONTINGENCIES:

The Company is involved in various legal claims and lawsuits in connection with its ordinary business operations. The Company intends to vigorously defend these claims. While the final outcome with respect to any actions or claims outstanding or pending as of March 31, 2015 cannot be predicted with certainty, management does not believe that the resolution of these claims, individually or in the aggregate, will have a material adverse effect on the Company's financial position.

14. STOCKHOLDERS' EQUITY:

The following unaudited table summarizes stockholders' equity transactions for the three month period ended March 31, 2015:

	Common stock Number	Amount	Additional paid in capital	Deficit	Accumulated other comprehensive income	Total stockholders equity
Balance, December 31, 2014	11,329,732	\$ 14,130,059	\$ 29,090,058	\$(6,955,283)	\$(622,441)) \$ 35,642,393
Exercise of stock options	74,997	360,949	(112,966)	-	-	247,983
Repurchase and retirement of shares	(407,996)	(516,003)	(7,196,142)	-	-	(7,712,145)
Stock-based compensation	-	-	125,048	-	-	125,048
Income tax effect related to stock options exercised	-	-	412,642	-	-	412,642
Net income for the period	-	-	-	2,833,943	-	2,833,943
Unrealized loss on foreign currency forward contracts treated as hedges	-	-	-	-	(960,866)	(960,866)
Reclassification to net income due to settlement of foreign currency forward contracts treated as hedges	-	-	-	-	416,074	416,074
Balance, March 31, 2015	10,996,733	\$ 13,975,005	\$ 22,318,640	\$(4,121,340)	\$(1,167,233)) \$ 31,005,072

On January 8, 2015, the Company announced that it successfully concluded a modified “Dutch auction tender offer” that was previously announced on December 8, 2014. Under the terms of the offer, the Company repurchased an aggregate of 193,907 shares of its common stock at a purchase price of \$18.50 per share, for a total of \$3,587,280, excluding transaction costs of approximately \$70,000. The purchase price and all transaction costs were funded from available cash. All shares purchased in the tender offer received the same price and all shares repurchased were immediately retired. As a result of the completion of the tender offer, as of January 7, 2015, the Company had 11,135,825 shares issued and outstanding.

On February 11, 2015, the Company announced that its Board of Directors has approved a stock buyback program to repurchase up to \$20 million of its common stock in the open market. Purchases will be made exclusively through the facilities of the NASDAQ Capital Market. The stock buyback program commenced on February 16, 2015 and will terminate on or before February 15, 2016. The Company repurchased 214,089 shares under this program during the three months ended March 31, 2015 for a total of \$4,055,056.

On March 5, 2014, the Company announced a stock buyback program. Under this buyback program, the Company may repurchase up to \$20 million of the Company's common stock over the 12-month period that commenced on March 4, 2014. The Company repurchased 6,092 shares under this program during the three months ended March 31, 2014 for a total of \$82,286.

15. SHARE-BASED PAYMENTS

(a) Stock options

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model, consistent with the guidance on stock compensation. Because option-pricing models require the use of subjective assumptions, changes in these assumptions can materially affect the fair value of the options. The assumptions presented in the table below represent the weighted average of the applicable assumption used to value stock options at their grant date. The Company calculates expected volatility based on historical volatility of the Company's common shares. The expected term, which represents the period of time that options granted are expected to be outstanding, is estimated based on historical exercise experience. The Company evaluated historical exercise behavior when determining the expected term assumptions. The risk-free rate assumed in valuing the options is based on the U.S. Treasury yield curve in effect at the time of grant for the expected term of the option. The Company determines the expected dividend yield percentage by dividing the expected annual dividend by the market price of our common shares at the date of grant.

Details of stock option transactions for the three months ended March 31, 2015 and March 31, 2014 are as follows:

	Three months ended		Three months ended	
	March 31, 2015		March 31, 2014	
	Weighted		Weighted	
	Number of	Average exercise price	Number of	Average exercise price
	Shares	per share	Shares	per share
Outstanding, beginning of period	976,062	\$ 5.41	1,407,639	\$ 3.80
Granted	45,000	19.41	—	—
Exercised	(74,997)	3.31	(291,913)	3.12
Forfeited	(2,742)	12.15	(5,594)	5.56
Expired	—	—	(2,875)	3.40
Outstanding, end of period	943,323	\$ 6.23	1,107,257	\$ 3.97
Options exercisable, end of period	653,145	\$ 4.11	753,506	\$ 3.15

As of March 31, 2015, the exercise prices, weighted average remaining contractual life and intrinsic values of outstanding options were as follows:

			Options outstanding			Options exercisable			
			Weighted	Weighted		Weighted			
Exercise price				average	Average	Aggregate			
				exercise	remaining	intrinsic			
				Number			Number	average	Aggregate
				price per	contractual	value	exercisable	exercise	intrinsic
			share	life (years)		share			
\$2.40	-	\$2.92	467,410	\$ 2.73	1.9	\$7,605,899	443,444	\$ 2.72	\$7,220,526
\$3.00	-	\$5.76	213,312	\$ 5.09	3.5	2,967,841	139,685	\$ 4.85	1,976,136
\$8.56	-	\$10.16	119,126	\$ 9.12	5.0	1,176,925	43,141	\$ 9.06	428,645
\$14.67	-	\$19.41	143,475	\$ 16.92	6.0	317,281	26,875	\$ 15.37	97,469
			943,323	\$ 6.23	3.2	\$12,067,946	653,145	\$ 4.11	\$9,722,776

Total unrecognized compensation cost relating to unvested stock options at March 31, 2015, prior to the consideration of expected forfeitures, was approximately \$1,228,825 and is expected to be recognized over a weighted average period of 2.4 years.

The Company recorded stock-based compensation of \$125,048 and \$100,977 for the three months ended March 31, 2015 and 2014, respectively.

The Company has not capitalized any stock-based compensation expense as part of the cost of an asset.

16. FAIR VALUE MEASUREMENT

ASC Topic 820, “*Fair Value Measurements and Disclosures*” establishes a valuation hierarchy for disclosure of the inputs to valuation used to measure fair value. This hierarchy prioritizes the inputs into three broad levels. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are quoted prices for similar assets and liabilities in active markets or inputs that are observable for the asset or liability, either directly or indirectly through market corroboration, for substantially the full term of the financial instrument. Level 3 inputs are unobservable inputs based on the Company's own assumptions used to measure assets and liabilities at fair value. A financial asset or liability's classification within the hierarchy is determined based on the lowest level input that is significant to the fair value measurement.

The following table provides a summary of the fair values of the Company's derivative instrument assets and liabilities measured at fair value on a recurring basis at March 31, 2015:

	March 31, 2015			
	Fair Value		Liabilities	
	Measurements Using		at	
	Level 1	Level 2	Level 3	Fair Value
Derivative instrument liability	\$—	\$2,139,268	\$ —	\$2,139,268
Total Liabilities	\$—	\$2,139,268	\$ —	\$2,139,268

The following table provides a summary of the fair values of the Company's derivative instrument assets measured at fair value on a recurring basis as at December 31, 2014:

December 31, 2014				
	Fair Value			Liabilities
	Measurements Using			at
	Level 1	Level 2	Level 3	Fair Value
Derivative instrument liability	\$—	\$1,115,805	\$ —	\$1,115,805
Total Liabilities	\$—	\$1,115,805	\$ —	\$1,115,805

The carrying values of cash and cash equivalents, accounts receivable, accounts payable, accreditation fees payable, customer deposits, loan payable and accrued liabilities approximate their fair values due to the relatively short periods to maturity of the instruments.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains, in addition to historical information, forward-looking statements by us with regard to our expectations as to financial results and other aspects of our business that involve risks and uncertainties and may constitute forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Words such as “may,” “should,” “anticipate,” “believe,” “plan,” “estimate,” “expect”, “intend” and other expressions are intended to identify forward-looking statements. The forward-looking statements contained in this report include statements regarding, among other things, the Company's foreign currency requirements, specifically for the Canadian dollar; Ting mobile subscriber growth and retention rates, the number of new, renewed and transferred-in domain names we register as our business develops and competes; the effect of a potential global top level domain (“gTLD”) expansion by the Internet Corporation for Assigned Names and Numbers (“ICANN”) on the number of domains we register and the impact it may have on related revenues; our belief that the market for domain name registration will trend upward gradually and may be affected by market volatility; our belief that, by increasing the number of services we offer, we will be able to generate higher revenues; the revenue that our parked page vendor relationships may generate in the future; the effectiveness of our intellectual property protection, including our ability to license proprietary rights to network partners and to register additional trademarks and service marks; the potential impact of current and pending claims on our business; our valuations of certain deferred tax assets; our expectation to collect our outstanding receivables, net of our allowance for doubtful accounts; our expectation regarding fluctuations in certain expense and cost categories; our expectations regarding our unrecognized tax benefit and the timing or completion of certain audits of our US, Canadian and German tax returns; our expectations regarding cash from operations to fund our business; our expectation regarding increased competition due to the introduction of new gTLDs by ICANN; the impact of cancellations of or amendments to market development fund programs under which we receive funds; and our belief that a slowing economy may lead to a decrease in advertising spending. These statements are based on management's current expectations and are subject to a number of uncertainties and risks that could cause actual results to differ materially from those described in the forward-looking statements. Many factors affect our ability to achieve our objectives and to successfully develop and commercialize our services including:

Changes in the nature of key strategic relationships with our Mobile Virtual Network Operator (“MVNO”) partners;

The effects of vigorous competition on a highly penetrated mobile telephony market, including the impact of competition on the price we are able to charge subscribers for services and devices and on the geographic areas served by our MVNO partner wireless networks;

Our ability to manage any potential increase in subscriber churn or bad debt expense;

Our ability to continue to generate sufficient working capital to meet our operating requirements;

Our ability to maintain a good working relationship with our vendors and customers;

The ability of vendors to continue to supply our needs;

Actions by our competitors;

Our ability to achieve gross profit margins at which we can be profitable;

Our ability to attract and retain qualified personnel in our business;

Our ability to effectively manage our business;

Our ability to obtain and maintain approvals from regulatory authorities on regulatory issues;

The effects of any material impairment of our goodwill or other indefinite-lived intangible assets;

Pending or new litigation; and

Factors set forth under the caption “Item 1A Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended December 31, 2014.

This list of factors that may affect our future performance and financial and competitive position and also the accuracy of forward-looking statements is illustrative, but it is by no means exhaustive. Accordingly, all forward-looking statements should be evaluated with the understanding of their inherent uncertainty. All forward-looking statements included in this document are based on information available to us as of the date of this document, and we assume no obligation to update these cautionary statements or any forward-looking statements except to the extent of any obligations under the Securities Exchange Act of 1934 or the Securities Act of 1933. These statements are not guarantees of future performance.

We qualify all the forward-looking statements contained in this Quarterly Report on Form 10-Q by the foregoing cautionary statements.

OVERVIEW

Our mission is to provide simple useful services that help people unlock the power of the Internet. We accomplish this by reducing the complexity our customers' experience as they acquire, deliver or use the Internet or Internet services such as domain name registration, email and other Internet services. We are organized and managed based on two service offerings, Domain Services and Network Access Services, which are differentiated primarily by their services, the markets they serve and the regulatory environments in which they operate.

Our principal place of business is located in Canada. We report our financial results as two operating segments, Domain Services, which derives revenue from three distinct service offerings – Wholesale, Retail and Portfolio, and Network Access Services, which derives revenue from the sale of retail mobile phones and services to individuals and small businesses. Our chief operating decision maker regularly reviews our operating results on a consolidated basis, principally to make decisions about how we utilize our resources and to measure our consolidated operating performance. To assist us in forecasting growth and to help us monitor the effectiveness of our operational strategies, our chief operating decision maker regularly reviews revenue for each of our service offerings in order to gain more depth and understanding of the key business metrics driving our business. Accordingly, we report Domain Services and Network Access Services revenue separately.

Domain Services

Domain Services include wholesale and retail domain name registration services, value added services and portfolio services. We earn revenues primarily from the registration fees charged to resellers in connection with new, renewed and transferred domain name registrations; the sale of retail Internet domain name registration and email services to individuals and small businesses; and by making our portfolio of domain names available for sale or lease. Domain Services revenues are attributed to the country in which the contract originates, primarily Canada.

Our primary distribution channel is a global network of more than 13,000 resellers in more than 100 countries who typically provide their customers, the end-users of the Internet, with a critical component for establishing and maintaining an online presence. Our primary focus is serving the needs of this network of resellers by providing superior services, easy-to-use interfaces, proactive and attentive customer service, reseller-oriented technology and agile design and development processes. We seek to provide superior customer service to our resellers by anticipating

their business needs and technical requirements. This includes providing easy-to-use interfaces that enable resellers to quickly and easily integrate our services into their individual business processes, and offering brandable end-user interfaces that emphasize simplicity and visual appeal. We also provide “second tier” support to our resellers by email and phone in the event resellers experience issues or problems with our services. In addition, our Network Operating Center provides proactive support to our resellers by monitoring all services and network infrastructure to address deficiencies before customer services are impacted.

We believe that the underlying platforms for our services are among the most mature, reliable and functional reseller-oriented provisioning and management platforms in our industry, and we continue to refine, evolve and improve these services for both resellers and end-users.

Wholesale, primarily branded as OpenSRS, derives revenue from its Domain Service and from providing Value-Added Services. The OpenSRS Domain Service manages 13.5 million domain names under the Tucows ICANN registrar accreditation and for other registrars under their own accreditations. Value-Added Services include hosted email which provides email delivery and webmail access to millions of mailboxes, Internet security services, publishing tools and reseller billing services. All of these services are made available to end-users through a network of over 13,000 web hosts, Internet service providers (“ISPs”), and other resellers around the world. In addition, we also derive revenue from the bulk sale of domain names and advertising from the OpenSRS Domain Expiry Stream.

Retail, primarily our Hover website, derives revenues from the sale of domain name registration and email services to individuals and small businesses. Retail also includes our Personal Names Service – based on over 40,000 surname domains – that allows roughly two-thirds of Americans to purchase an email address based on their last name.

Portfolio generates advertising revenue from our domain name portfolio and from our advertising-supported website, tucows.com. We also generate revenue by offering names in our domain portfolio for resale via our reseller network and other channels. In addition, we generate revenue from the payments for the sale of rights to gTLD strings under the New gTLD program.

Network Access Services

Network Access Services derives revenue from the sale of retail mobile phones and services to individuals and small businesses through the Ting website, as well as provides high speed Internet access, Internet hosting and network consulting to customers in Central Virginia through its acquisition of a 70% share in Ting Virginia on February 27, 2015. Ting provides customers with access to our provisioning and management tools to enable them, via the ting.com website, to purchase retail mobile phones and services. Revenues are generated in the United States and are provided on a monthly basis with no fixed contract term. Ting manages mobile telephony services for over 103,000 subscribers and has over 160,000 devices under management.

KEY BUSINESS METRICS

We regularly review a number of business metrics, including the following key metrics, to assist us in evaluating our business, measure the performance of our business model, identify trends impacting our business, determine resource allocations, formulate financial projections and make strategic business decisions. The following table sets forth, the key business metrics which we believe are the primary indicators of our performance for the periods presented:

Domain Services

Total new, renewed and transferred-in domain name registrations:

	Three months ended	
	March 31, 2015 (1) (in 000's)	2014 (1)
Total new, renewed and transferred-in domain name registrations	2,498	2,481

- (1) For a discussion of these period to period changes in the domains provisioned and how they impacted our financial results, see the Net Revenue discussion below.

Domain names under management:

	March 31,	
	2015	2014
	(1)	(1)
	(in 000's)	
Domain names under management:		
Registered using the Tucows Registrar Accreditation	10,203	10,550
Registered using our Resellers' Registrar Accreditations	3,345	3,622
Total domain names under management	13,548	14,182

- (1) For a discussion of these period to period changes in domains under management and how they impacted our financial results, see the Net Revenue discussion below.

Network Access Services

	March 31,	
	2015 (1)	2014
	(1)	(1)
	(in 000's)	
Ting subscribers under management	103,000	61,000
Ting devices under management	163,000	94,000

- (1) For a discussion of these period to period changes in subscribers and devices under management and how they impacted our financial results, see the Net Revenue discussion below.

OPPORTUNITIES, CHALLENGES AND RISKS

The increased competition in the market for Internet services in recent years, which we expect will continue to intensify in the short and long term, poses a material risk for us. As new registrars are introduced, existing competitors expand service offerings and competitors offer price discounts to gain market share, we face pricing pressure, which can adversely impact our revenues and profitability. To address these risks, we have focused on leveraging the scalability of our infrastructure and our ability to provide proactive and attentive customer service to aggressively compete to attract new customers and to maintain existing customers.

Substantially all of our Domain Services revenue is derived from domain name registrations and related value added services from wholesale and retail customers using our provisioning and management platforms. The market for wholesale registrar services is both price sensitive and competitive and is evolving with the introduction of New gTLDs, particularly for large volume customers, such as large web hosting companies and owners of large portfolios of domain names. We have a relatively limited ability to increase the pricing of domain name registrations without negatively impacting our ability to maintain or grow our customer base. Growth in our Domain Services revenue is dependent upon our ability to continue to attract and retain customers by maintaining consistent domain name registration and value added service renewal rates and to grow our customer relationships through refining, evolving and improving our provisioning platforms and customer service for both resellers and end-users. In addition, we also generate revenue through pay-per-click advertising and the sale of names from our portfolio of domain names and through the OpenSRS Domain Expiry Stream. The revenue associated with names sales and advertising has recently experienced flat to declining trends due to the uncertainty around the implementation of ICANN's New gTLD Program, lower traffic and advertising yields in the marketplace, which we expect to continue.

From time-to-time certain of our vendors provide us with Market Development Funds to expand or maintain the market position for their services. Any decision by these vendors to cancel or amend these programs for any reason may result in payments in future periods not being commensurate with what we have achieved during past periods.

Sales of domain names from our domain portfolio have a negative impact on our advertising revenue as these names are no longer available for advertising purposes. In addition, the timing of larger domain names portfolio sales is unpredictable and may lead to significant quarterly and annual fluctuations in our Portfolio revenue.

The communications industry continues to compete on the basis of network reach and performance, types of services and devices offered, and price.

As a MVNO our Ting service is reliant on our Mobile Network Operators "MNOs" providing competitive networks. Our MNOs each continue to invest in network expansion and modernization to improve their competitive positions.

Deployment of new and sophisticated technology on a very large scale entails risks. Should they fail to implement, maintain and expand their network capacity and coverage, adapt to future changes in technologies and continued access to and deployment of adequate spectrum successfully, our ability to provide wireless services to our subscribers, to retain and attract subscribers and to maintain and grow our subscriber revenues could be adversely affected, which would negatively impact our operating margins.

Ting has also enjoyed rapid growth in its first three years of operation. During this growth phase we have been able to continue to grow gross customer additions and maintain a consistent churn rate, which has allowed us to maintain net new customer additions despite the impact of churn on a fast growing customer base. We expect price competition to grow more intense in the industry which could result in increased customer churn or reductions of customer acquisition rates either of which could result in slower growth rates or in certain cases, our ability to maintain growth.

Our revenue is primarily realized in U.S. dollars and a major portion of our operating expenses are paid in Canadian dollars. Fluctuations in the exchange rate between the U.S. dollar and the Canadian dollar may have a material effect on our business, financial condition and results from operations. In particular, we may be adversely affected by a significant weakening of the U.S. dollar against the Canadian dollar on a quarterly and an annual basis. Our policy with respect to foreign currency exposure is to manage our financial exposure to certain foreign exchange fluctuations with the objective of neutralizing some or all of the impact of foreign currency exchange movements by entering into foreign exchange forward contracts to mitigate the exchange risk on a portion of our Canadian dollar exposure. We may not always enter into such forward contracts and such contracts may not always be available and economical for us. Additionally, the forward rates established by the contracts may be less advantageous than the market rate upon settlement.

Net Revenues

Domain Services

Wholesale - OpenSRS Domain Service

Historically, our OpenSRS Domain Service has constituted the largest portion of our business and encompasses all of our services as an accredited registrar related to the registration, renewal, transfer and management of domain names. In addition, this service fuels other revenue categories as it often is the initial service for which a reseller will engage us, enabling us to follow on with other services and allowing us to add to our portfolio by purchasing names registered through us upon their expiration.

We receive revenues for each domain registration or other Internet service processed through our system by Service Providers.

With respect to the sale of domain registrations, we earn registration fees in connection with each new, renewed and transferred-in registration and from providing provisioning services to Service Providers and registrars on a monthly basis. Domain registrations are generally purchased for terms of one to ten years. Payments for the full term of all services, or billed revenue, are received at the time of activation of service and where appropriate are recorded as deferred revenue and are recognized as earned ratably over the term of provision of service. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during the quarters and the year.

Wholesale – OpenSRS Value-Added Services

We derive revenue from our hosted email service through our global distribution network. Our hosted email service is offered on a per account, per month basis, and provides resellers with a reliable, scalable “white label” hosted email solution that can be customized to their branding and business model requirements. The hosted email service also includes spam and virus filtering on all accounts. End-users can access the hosted email service via a full-featured, multi-language AJAX-enabled web interface or through traditional desktop email clients, such as Microsoft Outlook or Apple Mail, using IMAP or POP/SMTP.

We also derive revenue from other Value-Added Services primarily from provisioning SSL and other trust certificates. In addition, we derive revenue from the bulk sale of domain names and advertising from the OpenSRS Domain Expiry Stream.

In addition, we provide billing, provisioning and customer care software solutions to ISPs through our Platypus billing software.

Retail – Hover

We derive revenues from Hover's sale of retail Internet domain name registration and email services to individuals and small businesses.

Portfolio

We derive revenue from our portfolio of domain names by displaying advertising on the domains and by making them available for sale or lease. When a user types one of these domain names into a web browser, they are presented with dynamically generated links that are pay-per-click advertising. Every time a user clicks on one of these links, it generates revenue for us through our partnership with third-parties who provide syndicated pay-per-click advertising (“parked page vendors”).

Our parked page vendor relationships may not continue to generate levels of revenue commensurate with what we have achieved during past periods. Our ability to generate online advertising revenue from parked page vendors depends on their advertising networks' assessment of the quality and performance characteristics of Internet traffic resulting from online advertisements rendered on their websites. We have no control over any of these quality assessments. Parked page vendors may from time to time change their existing, or establish new, methodologies and metrics for valuing the quality of Internet traffic and delivering pay-per-click advertisements. Any changes in these methodologies, metrics and advertising technology platforms could decrease the amount of revenue that we generate from online advertisements. In addition, parked page vendors may at any time change or suspend the nature of the service that they provide to online advertisers. These types of changes or suspensions would adversely impact our ability to generate revenue from pay-per-click advertising.

Portfolio names are sold through our premium domain name service, auctions or in negotiated sales. The size of our domain name portfolio varies over time, as we acquire and sell domains on a regular basis to maximize the overall value and revenue generation potential of our portfolio. In evaluating names for sale, we consider the potential foregone revenue from pay-per-click advertising, as well as other factors. The name will be offered for sale if, based on our evaluation, the name is deemed non-essential to our business and management believes that deriving proceeds from the sale is strategically more beneficial to the Company. In addition, we generate revenue from the payments for

the sale of rights to gTLD strings under ICANN's New gTLD Program.

Portfolio names that have been acquired from third-parties or through acquisition are included as intangible assets with indefinite lives on our consolidated balance sheet.

We also generate advertising and other revenue through our ad-supported content site, tucows.com. This site primarily derives revenue from banner and text advertising. In addition, their revenue is derived from software developers who rely on us as a primary source of distribution. Software developers use our Author Resource Center to submit their products for inclusion on our site and to purchase promotional placements of their software.

Network Access Services

Ting

We derive revenue from Ting's sale of retail mobile phones and services to individuals and small businesses. Ting provides customers with access to our provisioning and management tools to enable them, via the ting.com website, to purchase retail mobile phones and services. Revenues are generated in the United States and are provided on a monthly basis with no fixed contract term. In addition, with the acquisition of a 70% share in Ting Virginia on February 27, 2015, we began providing high speed Internet access, Internet hosting and network consulting to customers in Central Virginia.

Critical Accounting Policies

Preparation of our consolidated financial statements in accordance with U.S. GAAP requires us to make estimates and assumptions that affect the reported amounts of certain assets, liabilities, revenues and expenses, as well as related disclosure of contingent assets and liabilities. There have been no material changes to the critical accounting policies and estimates as previously disclosed in Part II, Item 7 of our Annual Report on Form 10-K for the year ended December 31, 2014. For further information on our critical accounting policies and estimates, see Note 2 to the consolidated financial statements appearing in Part I, Item 1 in this Quarterly Report on Form 10-Q.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED MARCH 31, 2015 AS COMPARED TO THE THREE MONTHS ENDED MARCH 31, 2014

NET REVENUES

The following table presents our net revenues, by revenue source:

	Three months ended March 31,	
	2015	2014
<u>Domain Services:</u>		
Wholesale		
Domain Services	\$21,175,131	\$21,648,954
Value Added Services	2,241,998	2,603,605
Total Wholesale	23,417,129	24,252,559
Retail	2,875,728	2,384,063
Portfolio	1,247,962	1,053,640
Total Domain Services	27,540,819	27,690,262
<u>Network Access Services:</u>		
Ting	12,927,014	6,712,132
Total Network Access Services	12,927,014	6,712,132
	\$40,467,833	\$34,402,394
Increase over prior period	\$6,065,439	
Increase - percentage	18	%

The following table presents our revenues, by revenue source, as a percentage of total revenues:

	Three months ended March 31,	
	2015	2014
<u>Domain Services:</u>		
Wholesale		

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Domain Services	52 %	62 %
Value Added Services	6 %	8 %
Total Wholesale	58 %	70 %

Retail	7 %	7 %
Portfolio	3 %	3 %
Total Domain Services	68 %	80 %

Network Access Services:

Ting	32 %	20 %
Total Network Access Services	32 %	20 %

100% 100 %

Total net revenues for the three months ended March 31, 2015 increased by \$6.1 million or 18% to \$40.5 million when compared to the three months ended March 31, 2014.

Deferred revenue increased to \$73.3 million at March 31, 2015 from \$72.8 million at March 31, 2014 and increased by \$2.2 million from \$71.1 million at December 31, 2014.

No customer accounted for more than 10% of revenue during the three months ended March 31, 2015 and March 31, 2014. At March 31, 2015 and at March 31, 2014, no customer accounted for more than 10% of accounts receivable. Significant management judgment is required at the time revenue is recorded to assess whether the collection of the resulting receivables is reasonably assured. On an ongoing basis we assess the ability of our customers to make required payments. Based on this assessment, we expect the carrying amount of our outstanding receivables, net of allowance for doubtful accounts, to be fully collected.

Wholesale

During the three months ended March 31, 2015, domain services revenue decreased by \$0.5 million to \$21.2 million when compared to the three months ended March 31, 2014.

During the three months ended March 31, 2015, the number of transactions from all new, renewed and transferred-in domain name registrations that we processed remained relatively flat at 2.4 million when compared to the three months ended March 31, 2014.

Domain services revenue and transaction volumes continue to be impacted by the ongoing migration of a handful of large, low margin customers. These customers have been moving their domain management and domain transaction processing to their own accreditations and in-house systems. We anticipate that the number of new, renewed and transferred-in domain name registrations will continue to be impacted by decisions large volume customers make with regard to acquiring their own accreditations and the impact that the significant expansion of the number of New gTLDs implementation of ICANN's New gTLD Program will have on the market. While we anticipate that the number of new, renewed and transferred-in domain name registrations will continue to incrementally increase in the long term, the volatility of these factors could affect the growth of domain names that we manage.

As of March 31, 2015, total domains that we manage under our own accreditation decreased to 10.2 million when compared to 10.6 million at March 31, 2014. These decreases in domains under management primarily resulted from the same factors impacting domain transactions mentioned above. Also, as of March 31, 2015, total domains that we manage on behalf of other accredited registrars decreased to 3.3 million when compared to 3.6 million at the end of March 31, 2014, primarily the result of a single customer that transitioned the customer's domain management platform to an in-house system in Fiscal 2014.

During the three months ended March 31, 2015, value added services revenue decreased by \$0.4 million to \$2.2 million when compared to the three months ended March 31, 2014. This decrease was primarily due to the decrease in revenue from pay-per-click advertising and the sale of names through the OpenSRS Domain Expiry Stream. The revenue associated with names sales and advertising has recently experienced flat to declining trends due to the uncertainty around the implementation of ICANN's New gTLD Program, lower traffic and advertising yields in the marketplace, which we expect to continue.

Retail

Net revenues from Retail for the three months ended March 31, 2015, as compared to the three months ended March 31, 2014, increased by \$0.5 million, or 21%, to \$2.9. This increase was largely due to the success that our retail marketing initiatives and improved websites are having on our ability to attract new customers and retain existing ones for Hover.

Portfolio

Net revenues from Portfolio for the three months ended March 31, 2015, as compared to the three months ended March 31, 2014, increased by \$0.2 million to \$1.2 million. This increase primarily related to gains we recognized on the sale of our minority interest in .store as a result of this contested domain being resolved through a confidential private auction in February 2015. This increase was partially offset by lower sales of big ticket domains. The market for monetization of domain names is rapidly evolving and is being impacted by uncertainty around the implementation of ICANN's New gTLD Program.

Network Access Services

Net revenues from Ting mobile phone and fixed Internet access services and equipment for the three months ended March 31, 2015, as compared to the three months ended March 31, 2014, increased by \$6.2 million or 93% to \$12.9 million. This increase primarily reflects the impact the larger subscriber base is having on service revenues. As of March 31, 2015, Ting had 103,000 subscribers and 163,000 mobile devices under its management compared to 61,000 subscribers and 94,000 devices under management as of March 31, 2014.

COST OF REVENUES

Wholesale

OpenSRS Domain Service

Cost of revenues for domain registrations represents the amortization of registry fees on a basis consistent with the recognition of revenues from our customers, namely ratably over the term of provision of the service. Registry fees, the primary component of cost of revenues, are paid in full when the domain is registered, and are initially recorded as prepaid domain registry fees. This accounting treatment reasonably approximates a recognition pattern that corresponds with the provision of the services during the period. Market development funds that do not meet the criteria for revenue recognition under ASC 605-50 “Customer Payments and Incentives”, are reflected as cost of goods sold and are recognized as earned.

Value-Added Services

Costs of revenues for Value-Added Services include licensing and royalty costs related to the provisioning of certain components of hosted email, fees paid to third-party service providers, primarily for trust certificates and for printing services in connection with Platypus. Fees payable for trust certificates are amortized on a basis consistent with the provision of service, generally one year, while email hosting fees and monthly printing fees are included in cost of revenues in the month they are incurred.

Retail

Costs of revenues for our provision and management of Internet services through our retail site, Hover.com, include the amortization of registry fees on a basis consistent with the recognition of revenues from our customers, namely ratably over the term of provision of the service. Registry fees, the primary component of cost of revenues, are paid in full when the domain is registered, and are recorded as prepaid domain registry fees.

Portfolio

Costs of revenues for Portfolio represent the amortization of registry fees for domains added to our Portfolio over the renewal period, which is generally one year and the value attributed under intangible assets to any domain name sold. Payments for domain registrations are payable for the full term of service at the time of activation of service and are recorded as prepaid domain registry fees and are expensed ratably over the renewal term.

Costs of revenues for our ad-supported content site includes the fees paid to third-party service providers, primarily for digital certificates sold through our content sites and content license fees.

Network Access Services

The costs of revenue for Ting's mobile phone and fixed Internet access service include hardware (the cost of devices sold to our customers, order fulfillment related expenses and inventory write-downs) and network services (primarily our customers' voice, messaging and data usage) provided by our Mobile Network Operators.

Network costs

Network costs include personnel and related expenses, depreciation and amortization, communication costs, equipment maintenance, stock-based compensation and employee and related costs directly associated with the management and maintenance of our network. Communication costs include bandwidth, co-location and provisioning costs we incur to support the supply of all our services.

The following table presents our cost of revenues, by revenue source:

	Three months ended March 31,	
	2015	2014
<u>Domain Services:</u>		
Wholesale		
Domain Services	\$17,548,027	\$18,235,215
Value Added Services	536,132	540,722
Total Wholesale	18,084,159	18,775,937
Retail	1,220,500	1,015,416
Portfolio	171,558	243,855
Total Domain Services	19,476,217	20,035,208
<u>Network Access Services:</u>		
Ting	7,345,157	4,281,431
Total Network Access Services	7,345,157	4,281,431
<u>Network Expenses:</u>		
Network, other costs	1,222,096	1,143,644
Network, depreciation and amortization costs	203,566	182,974
Total Network Expenses	1,425,662	1,326,618
	\$28,247,036	\$25,643,257
Increase over prior period	\$2,603,779	
Increase - percentage	10	%

The following table presents our cost of revenues, as a percentage of total revenues:

	Three months ended March 31,	
	2015	2014
<u>Domain Services:</u>		
Wholesale		
Domain Services	43 %	53 %
Value Added Services	1 %	2 %
Total Wholesale	44 %	55 %

Retail	3	%	3	%
Portfolio	1	%	1	%
Total Domain Services	48	%	59	%

Network Access Services:

Ting	18	%	12	%
Total Network Access Services	18	%	12	%

Network Expenses:

Network, other costs	3	%	3	%
Network, depreciation and amortization costs	1	%	1	%
Total Network Expenses	4	%	4	%
	70	%	75	%

Total cost of revenues for the three months ended March 31, 2015 increased by \$2.6 million, or 10%, to \$28.2 million when compared to the three months ended March 31, 2014. This increase was primarily the result of increased network access service expenses due to the impact Ting's larger subscriber base is having on service costs.

Prepaid domain registration and other Internet services fees as of March 31, 2015 remained essentially flat at \$57.8 million when compared to March 31, 2014.

Wholesale

Costs for Wholesale for the three months ended March 31, 2015 decreased by \$0.7 million, or 4%, to \$18.1 million and when compared to the three months ended March 31, 2014. This reduction in costs is primarily the result of an ongoing shift in product mix to higher margin domain services and with growth in the core wholesale domain services business being off-set with a handful of large clients migrating their business to their own accreditations.

Retail

Costs for Retail for the three months ended March 31, 2015 increased by \$0.2 million, to \$1.2 million when compared to the three months ended March 31, 2014. These increases resulted primarily from the increased cost of additional volume in Hover services.

Portfolio

Costs for Portfolio for the three months ended March 31, 2015 decreased by \$0.1 million, to \$0.2 million when compared to the three months ended March 31, 2014.

Network Access Services

Costs for Network Access Services for the three months ended March 31, 2015 increased by \$3.1 million, to \$7.3 million when compared to the three months ended March 31, 2014. This increase primarily reflects the impact the larger subscriber base is having on service costs.

Network Costs

Network costs before depreciation and amortization for the three months ended March 31, 2015 increased by \$0.1 million, to \$1.2 million when compared to the three months ended March 31, 2014.

SALES AND MARKETING

Sales and marketing expenses consist primarily of personnel costs. These costs include commissions and related expenses of our sales, product management, public relations, call center, support and marketing personnel. Other sales and marketing expenses include customer acquisition costs, advertising and other promotional costs.

	Three months ended			
	March 31,			
	2015		2014	
Sales and marketing	\$3,799,175		\$4,021,774	
Decrease over prior period	\$(222,599)			
Decrease - percentage	(6)%		
Percentage of net revenues	9	%	12	%

Sales and marketing expenses for the three months ended March 31, 2015 decreased by \$0.2 million, or 6%, to \$3.8 million when compared to the three months ended March 31, 2014. This decrease related primarily to increased workforce related expenses of \$0.2 million incurred in acquiring and servicing Ting subscribers being offset by a lower marketing spend, primarily the result of our decision last year to experiment with broader advertising initiatives as a means of accelerating our brand awareness and consideration.

TECHNICAL OPERATIONS AND DEVELOPMENT

Technical operations and development expenses consist primarily of personnel costs and related expenses required to support the development of new or enhanced service offerings and the maintenance and upgrading of existing infrastructure. This includes expenses incurred in the research, design and development of technology that we use to register domain names, network access services, email, retail, domain portfolio and other Internet services, as well as to distribute our digital content services. All technical operations and development costs are expensed as incurred.

	Three months ended			
	March 31,			
	2015		2014	
Technical operations and development	\$1,114,195		\$1,089,898	
Increase over prior period	\$24,297			
Increase - percentage	2	%		
Percentage of net revenues	3	%	3	%

Technical operations and development expenses for the three months ended March 31, 2015 remained essentially flat at \$1.1 million when compared to the three months ended March 31, 2014.

GENERAL AND ADMINISTRATIVE

General and administrative expenses consist primarily of compensation and related costs for managerial and administrative personnel, fees for professional services, public listing expenses, rent, foreign exchange and other general corporate expenses.

	Three months ended			
	March 31,			
	2015	2014		
General and administrative	\$1,815,188	\$1,767,800		
Increase over prior period	\$47,388			
Increase - percentage	3	%		
Percentage of net revenues	4	%	5	%

General and administrative expenses for the three months ended March 31, 2015 increased slightly to \$1.8 million when compared to the three months ended March 31, 2014. This increase was primarily the result of increased credit card processing fees and bad debts primarily related to the growth of Ting of \$0.2 million when compared to the three months ended March 31, 2014. In addition, during the three months ended March 31, 2015, we recognized a gain on realized foreign exchange of \$0.8 million compared to a gain of \$0.5 million during the three months ended March 31, 2014. These gains were partially offset by our incurring a loss on foreign exchange revaluation of our foreign denominated assets and liabilities of \$0.4 million during the three months ended March 31, 2015 compared to a loss of \$0.2 million during the three months ended March 31, 2014.

DEPRECIATION OF PROPERTY AND EQUIPMENT

	Three months ended March 31,			
	2015	2014		
Depreciation of property and equipment	\$59,262	\$56,304		
Increase over prior period	\$2,958			
Increase - percentage	5	%		
Percentage of net revenues	0	%	0	%

Depreciation costs remained relatively flat at \$0.1 million for the three months ended March 31, 2015 and March 31, 2014, respectively.

AMORTIZATION OF INTANGIBLE ASSETS

	Three months ended	
	March 31,	
	2015	2014
Amortization of intangible assets	\$53,215	\$219,030
(Decrease) increase over prior period	\$(165,815)	
Decrease - percentage	(76)%
Percentage of net revenues	0	