

TUCOWS INC /PA/
Form 10-Q
August 10, 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 June 30, 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 (I.R.S. Employer
Incorporation or Organization) 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 August 6, 2015, there were 11,100,851 outstanding shares of common stock, no par value, of the registrant.

TUCOWS INC.

Form 10-Q Quarterly Report

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PART I

FINANCIAL INFORMATION

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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)**

| | June 30, 2015 (unaudited) | December 31, 2014 |
|--|--|----------------------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 15,300,762 | \$ 8,271,377 |
| Accounts receivable, net of allowance for doubtful accounts of \$122,953 as of June 30, 2015 and \$125,766 as of December 31, 2014 | 8,208,238 | 6,789,685 |
| Inventory | 619,413 | 393,774 |
| Prepaid expenses and deposits | 5,678,128 | 3,697,292 |
| Prepaid domain name registry and ancillary services fees, current portion | 46,922,331 | 44,614,858 |
| Other assets (note 5) | - | 8,199,000 |
| Deferred tax asset, current portion (note 9) | 3,316,406 | 2,498,196 |
| Income taxes recoverable | 227,759 | 997 |
| Total current assets | 80,273,037 | 74,465,179 |
| Prepaid domain name registry and ancillary services fees, long-term portion | 11,676,068 | 11,764,765 |
| Property and equipment | 6,156,918 | 1,609,787 |
| Deferred tax asset, long-term portion (note 9) | 5,417,090 | 4,880,423 |
| Intangible assets (note 7) | 14,768,934 | 14,202,585 |
| Goodwill (note 7) | 21,005,143 | 18,873,127 |
| Total assets | \$ 139,297,190 | \$ 125,795,866 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 3,777,159 | \$ 3,579,920 |
| Accrued liabilities | 5,274,863 | 3,941,549 |
| Customer deposits | 4,914,645 | 4,461,727 |

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| | | |
|---|----------------|----------------|
| Derivative instrument liability, (note 6) | 1,374,202 | 1,115,805 |
| Deferred rent, current portion | 10,783 | - |
| Loan payable (note 8) | 3,500,000 | - |
| Deferred revenue, current portion | 58,633,546 | 55,495,566 |
| Accreditation fees payable, current portion | 503,644 | 466,201 |
| Deferred tax liability, current portion (note 9) | 24,765 | - |
| Income taxes payable (note 9) | 1,483,258 | 473,480 |
| Total current liabilities | 79,496,865 | 69,534,248 |
| Derivative instrument liability, long-term portion (note 6) | 149,445 | - |
| Deferred revenue, long-term portion | 15,639,306 | 15,610,753 |
| Accreditation fees payable, long-term portion | 122,846 | 128,243 |
| Deferred rent, long-term portion | 92,642 | 92,878 |
| Other liabilities (note 10) | 1,545,832 | - |
| Deferred tax liability, long-term portion (note 9) | 5,015,677 | 4,787,351 |
| Redeemable non-controlling interest (note 4) | 3,012,150 | - |
| 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; 11,083,976 shares issued and outstanding as of June 30, 2015 and 11,329,732 shares issued and outstanding as of December 31, 2014 | 14,411,616 | 14,130,059 |
| Additional paid-in capital | 22,492,630 | 29,090,058 |
| Deficit | (1,848,495) | (6,955,283) |
| Accumulated other comprehensive income (loss) | (833,324) | (622,441) |
| Total stockholders' equity | 34,222,427 | 35,642,393 |
| Total liabilities and stockholders' equity | \$ 139,297,190 | \$ 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 June 30, | | Six months ended June 30, | |
|--|------------------------------------|--------------|----------------------------------|--------------|
| | 2015 | 2014 | 2015 | 2014 |
| Net revenues (note 12) | \$42,889,220 | \$35,588,001 | \$83,357,053 | \$69,990,395 |
| Cost of revenues (note 12): | | | | |
| Cost of revenues | 28,250,672 | 24,736,004 | 55,072,046 | 49,052,643 |
| Network expenses | 1,494,838 | 1,144,697 | 2,716,934 | 2,288,341 |
| Depreciation of property and equipment | 279,929 | 173,963 | 479,571 | 356,937 |
| Amortization of intangible assets (note 7) | 11,532 | - | 15,456 | - |
| Total cost of revenues | 30,036,971 | 26,054,664 | 58,284,007 | 51,697,921 |
| Gross profit | 12,852,249 | 9,533,337 | 25,073,046 | 18,292,474 |
| Expenses: | | | | |
| Sales and marketing | 4,847,963 | 3,762,441 | 8,647,138 | 7,784,215 |
| Technical operations and development | 1,189,276 | 1,107,532 | 2,303,471 | 2,197,430 |
| General and administrative | 2,173,254 | 1,886,319 | 3,988,442 | 3,654,119 |
| Depreciation of property and equipment | 62,022 | 52,538 | 121,284 | 108,842 |
| Amortization of intangible assets (note 7) | 56,997 | 219,030 | 110,212 | 438,060 |
| Impairment of indefinite life intangible assets (note 7) | 37,805 | 326,457 | 50,298 | 577,145 |
| Loss on currency forward contracts (note 6) | 602,439 | 96,545 | 1,559,297 | 647,916 |
| Total expenses | 8,969,756 | 7,450,862 | 16,780,142 | 15,407,727 |
| Income from operations | 3,882,493 | 2,082,475 | 8,292,904 | 2,884,747 |
| Other income (expense): | | | | |
| Interest expense, net | (57,402) | (69,348) | (82,177) | (143,181) |
| Total other income (expense) | (57,402) | (69,348) | (82,177) | (143,181) |
| Income before provision for income taxes | 3,825,091 | 2,013,127 | 8,210,727 | 2,741,566 |
| Provision for income taxes (note 9) | 1,540,096 | 665,945 | 3,091,789 | 917,545 |
| Net income before redeemable non-controlling interest | 2,284,995 | 1,347,182 | 5,118,938 | 1,824,021 |

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| | | | | |
|---|-------------|-------------|-------------|-------------|
| Redeemable non-controlling interest | (49,985) | - | (71,467) | - |
| Net (earnings) loss attributable to redeemable non-controlling interest | 49,985 | - | 71,467 | - |
| Net income | 2,284,995 | 1,347,182 | 5,118,938 | 1,824,021 |
| Other comprehensive income (loss), net of tax | | | | |
| Gain (loss) on hedging activities | (38,046) | 285,136 | (998,912) | (165,382) |
| Net amount reclassified to earnings | 371,955 | 145,141 | 788,029 | 380,192 |
| Other comprehensive income (loss) net of tax of \$184,262 and \$224,137 for the three months ended June 30, 2015 and June 30, 2014 and \$135,616 and \$111,897 for the six months ended June 30, 2015 and June 30, 2014 | 333,909 | 430,277 | (210,883) | 214,810 |
| Comprehensive income for the period | \$2,618,904 | \$1,777,459 | \$4,908,055 | \$2,038,831 |
| Basic earnings per common share (note 11) | \$0.21 | \$0.12 | \$0.46 | \$0.16 |
| Shares used in computing basic earnings per common share (note 11) | 11,047,136 | 11,219,101 | 11,094,618 | 11,124,357 |
| Diluted earnings per common share (note 11) | \$0.20 | \$0.11 | \$0.44 | \$0.16 |
| Shares used in computing diluted earnings per common share (note 11) | 11,456,670 | 11,729,547 | 11,518,105 | 11,684,529 |

See accompanying notes to unaudited consolidated financial statements

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

| | Three months ended June 30, | | Six months ended June 30, | |
|--|------------------------------------|-------------|----------------------------------|--------------|
| | 2015 | 2014 | 2015 | 2014 |
| Cash provided by: | | | | |
| Operating activities: | | | | |
| Net income for the period | \$2,284,995 | \$1,347,182 | \$5,118,938 | \$1,824,021 |
| Items not involving cash: | | | | |
| Depreciation of property and equipment | 341,951 | 226,501 | 600,855 | 465,779 |
| Amortization of intangible assets | 68,529 | 219,030 | 125,668 | 438,060 |
| Impairment of indefinite life intangible asset | 37,805 | 326,457 | 50,298 | 577,145 |
| Deferred income taxes recovery | (801,919) | (415,246) | (966,169) | (758,477) |
| Excess tax benefits from share-based compensation expense | - | 594,899 | - | (418,901) |
| Amortization of deferred rent | 13,039 | 9,168 | 10,547 | 12,380 |
| Disposal of domain names | 11,357 | 7,247 | 17,685 | 8,869 |
| Loss (gain) on change in the fair value of forward contracts | (97,451) | (192,460) | 61,342 | (105,314) |
| Stock-based compensation | 124,605 | 85,357 | 249,653 | 186,334 |
| Change in non-cash operating working capital: | | | | |
| Accounts receivable | (1,088,453) | (350,806) | (1,257,038) | (1,613,727) |
| Inventory | (45,294) | 28,293 | (158,444) | (171,454) |
| Prepaid expenses and deposits | (592,614) | (259,698) | (1,892,392) | (626,534) |
| Prepaid domain name registry and ancillary services fees | (755,932) | (606,215) | (2,218,776) | (2,421,898) |
| Income taxes recoverable | 121,248 | (133,242) | 783,016 | (566,543) |
| Accounts payable | (109,990) | (866,473) | 7,576 | 803,942 |
| Accrued liabilities | 1,169,753 | 253,027 | 1,110,533 | (169,371) |
| Customer deposits | 589,361 | 16,054 | 452,918 | (13,075) |
| Deferred revenue | 983,586 | 867,445 | 3,045,096 | 3,616,378 |
| Accreditation fees payable | (18,981) | (21,755) | 32,046 | 28,332 |
| Net cash provided by operating activities | 2,235,595 | 1,134,765 | 5,173,352 | 1,095,946 |
| Financing activities: | | | | |
| Proceeds received on exercise of stock options | 299,472 | 130,782 | 547,455 | 1,041,863 |
| Excess tax benefits from share-based compensation expense | 676,060 | - | 1,088,702 | 1,013,800 |
| Repurchase of common stock | (489,536) | - | (8,201,681) | (82,286) |
| Proceeds received on loan payable | - | - | 3,500,000 | - |
| Repayment of loan payable | - | (325,000) | - | (941,667) |

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| | | | | |
|--|---------------|---------------|---------------|---------------|
| Net cash provided by / (used in) financing activities | 485,996 | (194,218) | (3,065,524) | 1,031,710 |
| Investing activities: | | | | |
| Additions to property and equipment | (1,149,020) | (313,281) | (1,340,782) | (382,026) |
| 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 | 50,000 | - | (357,493) | - |
| Net cash provided by (used in) investing activities | (1,099,020) | (313,281) | 4,921,557 | (382,026) |
| Increase in cash and cash equivalents | 1,622,571 | 627,266 | 7,029,385 | 1,745,630 |
| Cash and cash equivalents, beginning of period | 13,678,191 | 13,537,252 | 8,271,377 | 12,418,888 |
| Cash and cash equivalents, end of period | \$ 15,300,762 | \$ 14,164,518 | \$ 15,300,762 | \$ 14,164,518 |
| Supplemental cash flow information: | | | | |
| Interest paid | \$ 57,409 | \$ 69,437 | \$ 96,302 | \$ 143,386 |
| Income taxes paid, net | \$ 1,380,448 | \$ 588,916 | \$ 1,944,470 | \$ 1,258,540 |
| Supplementary disclosure of non-cash investing and financing activities: | | | | |
| Property and equipment acquired during the period not yet paid for | \$ 70,577 | \$ 19,637 | \$ 70,577 | \$ 19,637 |

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 provider of retail mobile phone service and fixed Internet access as well as a global distributor of Internet Services, such as domain name registration, digital certificates and email. The Company’s Internet Services are distributed through its global Internet-based distribution network of Internet service providers, web hosting companies and other companies that provide 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 June 30, 2015 and the results of operations and cash flows for the interim periods ended June 30, 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 June 30, 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, property and equipment and derivative financial instruments are included below:

(a) Revenue recognition

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's revenues are also derived from domain name registration fees on both a wholesale and retail basis, the sale of domain names, the provisioning of other Internet services, 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 provisioning 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.

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.

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.

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 and tools | 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, labor, 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.

(c) Derivative Financial Instruments

During the three and six months ended June 30, 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. RECENT ACCOUNTING PRONOUNCEMENTS:

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 was set to be effective for interim and annual periods beginning after December 15, 2016. On July 9, 2015, the FASB voted to defer the effective date by one year, such that the new standard will be effective for the Company for annual reporting periods beginning after December 15, 2017 (January 1, 2018 for the Company) and for interim reporting 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 does not intend to adopt the standard early and 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. 2015-03, *Interest - Imputation of Interest* (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs ("ASU 2015-03"). The amendments in ASU 2015-03 require that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. This guidance is effective for annual and interim reporting periods of public entities beginning after December 15, 2015, and early adoption is permitted. We do not expect the adoption of ASU 2015-03 to materially impact our consolidated financial statements.

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 the customer has the 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.

In July 2015, the FASB issued ASU No. 2015-11, *Simplifying the Measurement of Inventory* (Topic 330) ("ASU 2015-11"). The amendments in ASU 2015-11 require that inventory should be measured at the lower of cost and net realizable value. Net realizable value is the estimated selling prices in the ordinary course of business, less reasonably predictable cost of completion, disposal and transportation. This guidance is effective for annual and interim reporting periods of public entities beginning after December 15, 2016 (January 1, 2017 for the Company) and early adoption is permitted as of the beginning of an interim or annual reporting period. The implementation of the amendments in ASU 2015-11 are to be made on a prospective basis after the date of adoption. The Company is currently in the process of evaluating the impact that the adoption of ASU 2015-11 will have on its consolidated financial statements.

4. 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. On June 17, 2015, the final working capital adjustment was determined and \$50,000 was refunded from the escrow account to Ting Fiber, Inc. 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 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 was \$3,000,000 and is being accreted to the estimated liability amount using a discount rate of 5% over the periods of up to four years from the acquisition date. Subsequently, this amount was increased by \$12,150 to \$3,012,150 to reflect the present value of this Redeemable non-controlling interest as at June 30, 2015.

The purchase consideration is comprised as follows:

| | |
|------|-------------|
| Cash | \$3,135,140 |
|------|-------------|

| | |
|---|-------------|
| Less refund from working capital adjustment | (50,000) |
| Assumption of debt | 418,775 |
| Redeemable non-controlling interest | 3,000,000 |
| | \$6,503,915 |

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 | 2,132,016 |
| Net assets acquired | \$6,503,915 |

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 and six months ended June 30, 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:

| | Six months ended June 30, 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 June 30, 2015, is recorded as derivative instrument liabilities.

As of June 30, 2015, the notional amount of forward contracts that the Company held to sell U.S. dollars in exchange for Canadian dollars was \$24.0 million, of which \$20.4 million met the requirements of ASC Topic 815 and were designated as hedges (June 30, 2014 - \$13.5 million of which \$10.5 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 six months ended June 30, 2015, were as follows (amounts presented do not include any income tax effects).

Fair value of derivative instruments in the consolidated balance sheets

| | | As of | As of |
|--------------------|----------------------|--------------------|--------------------|
| | | June 30, | December |
| | | 2015 | 31, |
| | | Fair Value | 2014 |
| | | Fair Value | Fair Value |
| Derivatives | Balance Sheet | Asset | Asset |
| | Location | (Liability) | (Liability) |

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| | | |
|---|------------------------|------------------------------|
| Foreign currency forward contracts not designated as cash flow hedges | Derivative instruments | \$(230,472) \$(169,129) |
| Foreign currency forward contracts designated as cash flow hedges | Derivative instruments | \$(1,293,175) \$(946,676) |
| Total foreign currency forward contracts | Derivative instruments | \$(1,523,647) \$(1,115,805) |

8

Movement in Accumulated Other Comprehensive Income ("AOCI") balance for the three months ended June 30, 2015:

| | Gains and losses on cash flow hedges | Tax impact | Total AOCI |
|--|---|---------------|---------------|
| Opening AOCI balance – March 31, 2015 | \$(1,811,346) | \$644,113 | \$(1,167,233) |
| Other comprehensive income (loss) before reclassifications | (59,041) | 20,995 | (38,046) |
| Amount reclassified from accumulated other comprehensive income | 577,212 | (205,257) | 371,955 |
| Other comprehensive income (loss) for the three months ended June 30, 2015 | 518,171 | (184,262) | 333,909 |
| Ending AOCI balance – June 30, 2015 | \$(1,293,175) | \$459,851 | \$(833,324) |

Movement in Accumulated Other Comprehensive Income ("AOCI") balance for the six months ended June 30, 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 | (1,569,387) | 570,475 | (998,912) |
| Amount reclassified from accumulated other comprehensive income | 1,222,888 | (434,859) | 788,029 |
| Other comprehensive income (loss) for the six months ended June 30, 2015 | (346,499) | 135,616 | (210,883) |
| Ending AOCI balance – June 30, 2015 | \$(1,293,175) | \$459,851 | \$(833,324) |

Effects of derivative instruments on income and other comprehensive income (OCI) for the three months ended June 30, 2015 and June 30, 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) |
|---|---|---|---|---|---|
| Foreign currency forward contracts for the three months ended June 30, 2015 | \$ 333,909 | Operating expenses Cost of revenues | \$ (269,645) (102,310) | Operating expenses | \$ (8,741) |
| Foreign currency forward contracts for the three months ended June 30, 2014 | \$ 430,277 | Operating expenses Cost of revenues | \$ (200,756) (31,457) | Operating expenses | \$ — |

Effects of derivative instruments on income and other comprehensive income (OCI) for the six months ended June 30, 2015 and June 30, 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) |
|---|---|---|---|---|---|
| Foreign currency forward contracts for the six months ended June 30, 2015 | \$ (210,883) | Operating expenses Cost of revenues | \$ (571,235) (216,794) | Operating expenses | \$ (31,323) |
| Foreign currency forward contracts for the six months ended June 30, 2014 | \$ 214,810 | Operating expenses Cost of revenues | \$ (506,138) (72,101) | 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 gain of \$0.1 million for the change in fair value of outstanding contracts for the three months ended June 30, 2015, in the consolidated statement of operations and comprehensive income. The Company has recorded a loss of \$0.1 million upon settlement and a gain of \$0.2 million for the change in fair value of outstanding contracts for the three months ended June 30, 2014, in the consolidated statement of operations and comprehensive income.

The Company has recorded a loss of \$0.2 million upon settlement and a loss of \$0.1 million for the change in fair value of outstanding contracts for the six months ended June 30, 2015, in the consolidated statement of operations and comprehensive income. The Company has recorded a loss of \$0.2 million upon settlement and a gain of \$0.1 million for the change in fair value of outstanding contracts for the six months ended June 30, 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 Domainservices 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 Ting Virginia, 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 |
| Less refund on finalization of working capital adjustment | - | - | - | - | - | (50,000) | (50,000) |
| Balances, June 30, 2015 | \$ 2,044,847 | \$ 4,072,297 | \$ 5,801,040 | \$ 6,072,623 | \$ 882,320 | \$ 2,132,016 | \$ 21,005,143 |

The Company's goodwill relates 90% to its Domain Services operating segment and 10% to its Network Access 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

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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 June 30, 2015 is as follows:

| | Brand | Customer relationships | Network rights | Surname domain names indefinite life | Direct navigation domain names indefinite life | Total |
|--------------------------------|----------------|-------------------------------|-----------------------|---|---|---------------|
| | 7 years | 4 - 7 years | 15 years | | | |
| Net book value, March 31, 2015 | \$ 102,800 | \$ 647,715 | \$ 688,076 | \$ 11,516,213 | \$ 1,931,821 | \$ 14,886,625 |
| Sales of domain names | - | - | - | (1,947) | (9,410) | (11,357) |
| Impairment of domain names | - | - | - | (33,100) | (4,705) | (37,805) |
| Amortization expense | (7,710) | (49,287) | (11,532) | - | - | (68,529) |
| Net book value, June 30, 2015 | \$ 95,090 | \$ 598,428 | \$ 676,544 | \$ 11,481,166 | \$ 1,917,706 | \$ 14,768,934 |

A summary of acquired intangible assets for the six months ended June 30, 2015 is as follows:

| | Brand | Customer relationships | Network rights | Surname domain names indefinite life | Direct navigation domain names indefinite life | Total |
|---|----------------|-------------------------------|-----------------------|---|---|---------------|
| | 7 years | 4 - 7 years | 15 years | | | |
| 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 | - | - | - | (3,570) | (14,115) | (17,685) |
| Impairment of domain names | - | - | - | (40,888) | (9,410) | (50,298) |
| Amortization expense | (15,420) | (94,792) | (15,456) | - | - | (125,668) |
| Net book value, June 30, 2015 | \$ 95,090 | \$ 598,428 | \$ 676,544 | \$ 11,481,166 | \$ 1,917,706 | \$ 14,768,934 |

As of June 30, 2015, the accumulated amortization for the definite life intangibles was \$5.8 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 June 30, 2015, domain names, with a book value of \$37,805 (three months ended June 30, 2014 - \$0.3 million), were not renewed and were recorded as an impairment of indefinite life intangible assets. For the six months ended June 30, 2015, domain names, with a book value of \$50,298 (six months ended June 30, 2014 - \$0.6 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 (the “Tender Offer”, which was funded from available cash. Under the terms of the Tender 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 June 30, 2015, the outstanding balance under the 2012 DLR Loan was \$3.5 million (December 31, 2014 - Nil).

During the three months ended June 30, 2015 no amounts were drawn down on the 2012 DLRR Loan. At June 30, 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 June 30, 2015, the Company held contracts in the amount of \$24.0 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 June 30, 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, June 30, 2015, the Company was in compliance with these covenants. As at and for the period ended, June 30, 2014, the Company was in compliance with these covenants.

9. INCOME TAXES

For the three months ended June 30, 2015, the Company recorded a provision for income taxes of \$1.5 million on income before income taxes of \$3.8 million, using an estimated effective tax rate for the fiscal year ending December 31, 2015 (“Fiscal 2015”) adjusted for certain minimum state taxes. Comparatively, for the three months ended June 30, 2014, the Company recorded a provision for income taxes of \$0.7 million on income before taxes of \$2.0 million, using an estimated effective tax rate for the 2014 fiscal year.

For the six months ended June 30, 2015, the Company recorded a provision for income taxes of \$3.0 million on income before income taxes of \$8.2 million, using an estimated effective tax rate for Fiscal 2015 adjusted for certain minimum state taxes. Comparatively, for the six months ended June 30, 2014, the Company recorded a provision for income taxes of \$0.9 million on income before taxes of \$2.7 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 June 30, 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 June 30, 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 recognizing 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 June 30, 2015 | Three months ended June 30, 2014 | Six months ended June 30, 2015 | Six months ended June 30, 2014 |
|--|--|--|---|---|
| Numerator for basic and diluted earnings per common share: | | | | |
| Net income for the period | \$2,284,995 | \$1,347,182 | \$5,118,938 | \$1,824,021 |
| Denominator for basic and diluted earnings per common share: | | | | |
| Basic weighted average number of common shares outstanding | 11,047,136 | 11,219,101 | 11,094,618 | 11,124,357 |
| Effect of outstanding stock options | 409,534 | 510,446 | 423,487 | 560,172 |
| Diluted weighted average number of shares outstanding | 11,456,670 | 11,729,547 | 11,518,105 | 11,684,529 |
| Basic earnings per common share | \$0.21 | \$0.12 | \$0.46 | \$0.16 |
| Diluted earnings per common share | \$0.20 | \$0.11 | \$0.44 | \$0.16 |

For the three months ended June 30, 2015, outstanding options to purchase 45,000 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.

For the six months ended June 30, 2015, outstanding options to purchase 114,400 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 six months ended June 30, 2015, 193,907 common shares were repurchased and cancelled under the terms of the Tender Offer announced in December 2014.

During the three and six months ended June 30, 2015, 25,413 and 239,502 common shares respectively were repurchased and cancelled under the terms of our stock repurchase program announced in February 2015.

During the six months ended June 30, 2014, 6,092 common shares were repurchased and cancelled under the terms of our stock repurchase program announced in March 2014, none of which occurred during the quarter ended June 30,

2014.

The computation of earnings per share and diluted earnings per share for the three and six months ended June 30, 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 Network Access Services and Domain Services are described as follows:

1. 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.

2. 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.

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:

| Three months ended June 30, 2015 | Domain | Network | Consolidated |
|---|-----------------|-----------------|---------------------|
| | Name | Access | |
| | Services | Services | |
| | | | Totals |
| Net Revenues | \$27,471,251 | \$15,417,969 | \$ 42,889,220 |
| Cost of Revenues | 19,752,035 | 8,498,637 | 28,250,672 |
| Gross Profit before network expenses | 7,719,216 | 6,919,332 | 14,638,548 |
| Network expenses | | | 1,786,299 |
| Gross Profit | | | 12,852,249 |
| Expenses: | | | |
| Sales and marketing | | | 4,847,963 |
| Technical operations and development | | | 1,189,276 |
| General and administrative | | | 2,173,254 |
| Depreciation of property and equipment | | | 62,022 |
| Amortization of intangibles | | | 56,997 |
| Impairment of indefinite life intangible assets | | | 37,805 |
| Loss on currency forward contracts | | | 602,439 |
| Income from operations | | | 3,882,493 |
| Other expenses, net | | | 57,402 |
| Income before provision for income taxes | | | \$ 3,825,091 |

| Six months ended June 30, 2015 | Domain | Network | Consolidated |
|---|-----------------|-----------------|---------------------|
| | Name | Access | |
| | Services | Services | |
| | | | Totals |
| Net Revenues | \$55,012,070 | \$28,344,983 | \$ 83,357,053 |
| Cost of Revenues | 39,228,252 | 15,843,794 | 55,072,046 |
| Gross Profit before network expenses | 15,783,818 | 12,501,189 | 28,285,007 |
| Network expenses | | | 3,211,961 |
| Gross Profit | | | 25,073,046 |
| Expenses: | | | |
| Sales and marketing | | | 8,647,138 |
| Technical operations and development | | | 2,303,471 |
| General and administrative | | | 3,988,442 |
| Depreciation of property and equipment | | | 121,284 |
| Amortization of intangibles | | | 110,212 |
| Impairment of indefinite life intangible assets | | | 50,298 |

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| | |
|--|--------------|
| Loss on currency forward contracts | 1,559,297 |
| Income from operations | 8,292,904 |
| Other expenses, net | 82,177 |
| Income before provision for income taxes | \$ 8,210,727 |

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| Three months ended June 30, 2014 | Domain | Network | Consolidated |
|---|-----------------|-----------------|---------------------|
| | Name | Access | |
| | Services | Services | |
| Net Revenues | \$27,328,156 | \$8,259,845 | \$35,588,001 |
| Cost of Revenues | 19,696,030 | 5,039,974 | 24,736,004 |
| Gross Profit before network expenses | 7,632,126 | 3,219,871 | 10,851,997 |
| Network expenses | | | 1,318,660 |
| Gross Profit | | | 9,533,337 |
| Expenses: | | | |
| Sales and marketing | | | 3,762,441 |
| Technical operations and development | | | 1,107,532 |
| General and administrative | | | 1,886,319 |
| Depreciation of property and equipment | | | 52,538 |
| Amortization of intangibles | | | 219,030 |
| Write-off / impairment of indefinite life intangible assets | | | 326,457 |
| Loss on currency forward contracts | | | 96,545 |
| Income from operations | | | 2,082,475 |
| Other expenses, net | | | 69,348 |
| Income before provision for income taxes | | | \$2,013,127 |

| Six months ended June 30, 2014 | Domain | Network | Consolidated |
|---|-----------------|-----------------|---------------------|
| | Name | Access | |
| | Services | Services | |
| Net Revenues | \$55,018,418 | \$14,971,977 | \$69,990,395 |
| Cost of Revenues | 39,731,238 | 9,321,405 | 49,052,643 |
| Gross Profit before network expenses | 15,287,180 | 5,650,572 | 20,937,752 |
| Network expenses | | | 2,645,278 |
| Gross Profit | | | 18,292,474 |
| Expenses: | | | |
| Sales and marketing | | | 7,784,215 |
| Technical operations and development | | | 2,197,430 |
| General and administrative | | | 3,654,119 |
| Depreciation of property and equipment | | | 108,842 |
| Amortization of intangibles | | | 438,060 |
| Write-off / impairment of indefinite life intangible assets | | | 577,145 |
| Loss on currency forward contracts | | | 647,916 |
| Income from operations | | | 2,884,747 |
| Other expenses, net | | | 143,181 |
| Income before provision for income taxes | | | \$2,741,566 |

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

| | Three months ended June 30, | | Six months ended June 30, | |
|--|--|--------------|--------------------------------------|--------------|
| | 2015 | 2014 | 2015 | 2014 |
| <u>Domain Services:</u> | | | | |
| Wholesale | | | | |
| Domain Services | \$21,286,863 | \$21,503,086 | \$42,461,994 | \$43,152,040 |
| Value Added Services | 2,355,837 | 2,395,726 | 4,597,835 | 4,999,331 |
| Total Wholesale | 23,642,700 | 23,898,812 | 47,059,829 | 48,151,371 |
| Retail | 3,009,465 | 2,540,538 | 5,885,193 | 4,924,601 |
| Portfolio | 819,086 | 888,806 | 2,067,048 | 1,942,446 |
| Total Domain Services | 27,471,251 | 27,328,156 | 55,012,070 | 55,018,418 |
| <u>Network Access Services:</u> | | | | |
| Ting | 15,417,969 | 8,259,845 | 28,344,983 | 14,971,977 |
| Total Network Access Services | 15,417,969 | 8,259,845 | 28,344,983 | 14,971,977 |
| | \$42,889,220 | \$35,588,001 | \$83,357,053 | \$69,990,395 |

During the three and six months ended June 30, 2015 and 2014, no customer accounted for more than 10% of total revenue. As at June 30, 2015 two customers accounted for 21% of accounts receivable. At June 30, 2014, one customer accounted for 12% of accounts receivable.

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

| | Three months ended June 30, | | Six months ended June 30, | |
|--|--|--------------|--------------------------------------|--------------|
| | 2015 | 2014 | 2015 | 2014 |
| <u>Domain Services:</u> | | | | |
| Wholesale | | | | |
| Domain Services | \$17,749,516 | \$17,809,325 | \$35,297,543 | \$36,044,540 |
| Value Added Services | 501,518 | 563,011 | 1,037,650 | 1,103,733 |
| Total Wholesale | 18,251,034 | 18,372,336 | 36,335,193 | 37,148,273 |
| Retail | 1,322,620 | 1,110,659 | 2,543,120 | 2,126,075 |
| Portfolio | 178,381 | 213,035 | 349,939 | 456,890 |
| Total Domain Services | 19,752,035 | 19,696,030 | 39,228,252 | 39,731,238 |
| <u>Network Access Services:</u> | | | | |
| Ting | 8,498,637 | 5,039,974 | 15,843,794 | 9,321,405 |
| Total Network Access Services | 8,498,637 | 5,039,974 | 15,843,794 | 9,321,405 |
| <u>Network Expenses:</u> | | | | |
| Network, other costs | 1,494,838 | 1,144,697 | 2,716,934 | 2,288,341 |
| Network, depreciation and amortization costs | 291,461 | 173,963 | 495,027 | 356,937 |
| Total Network Expenses | 1,786,299 | 1,318,660 | 3,211,961 | 2,645,278 |
| | \$30,036,971 | \$26,054,664 | \$58,284,007 | \$51,697,921 |

(d) The following is a summary of the Company's property and equipment by geographic region:

| | June 30, | December |
|---------------|-----------------|-----------------|
| | 2015 | 31, |
| | | 2014 |
| Canada | \$1,245,594 | \$1,131,883 |
| United States | 4,840,253 | 379,891 |
| Germany | 71,071 | 98,013 |
| | \$6,156,918 | \$1,609,787 |

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

| | June 30, | December |
|---------------|-----------------|-----------------|
| | 2015 | 31, |
| | | 2014 |
| United States | \$736,992 | \$— |
| Germany | 633,070 | 735,730 |
| | \$1,370,062 | \$735,730 |

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

| | June 30, | December |
|--------|-----------------|-----------------|
| | 2015 | 31, |
| | | 2014 |
| Canada | \$8,733,496 | \$7,378,619 |
| | \$8,733,496 | \$7,378,619 |

(g) Valuation and qualifying accounts:

| | Balance | Charged to | Write-offs | Balance |
|---|------------------|--------------------|-------------------|----------------|
| | at | (recovered) | during | at |
| | beginning | costs and | period | end of |
| | period | expenses | period | period |
| Allowance for doubtful accounts, excluding provision for credit notes | | | | |
| Six months ended June 30, 2015 | \$ 125,766 | \$ 2,813 | \$ — | \$ 122,953 |
| 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 June 30, 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 June 30, 2015:

| | Common stock Number | Amount | Additional paid in capital | Deficit | Accumulated other comprehensive income | Total stockholders equity |
|--|--------------------------------|---------------|---|----------------|---|--|
| Balance, March 31, 2015 | 10,996,733 | \$ 13,975,005 | \$ 22,318,640 | \$(4,121,340) | \$(1,167,233) | \$ 31,005,072 |
| Exercise of stock options | 112,656 | 469,394 | (169,922) | - | - | 299,472 |
| Repurchase and retirement of shares | (25,413) | (32,783) | (456,753) | - | - | (489,536) |
| Stock-based compensation | - | - | 124,605 | - | - | 124,605 |
| Income tax effect related to stock options exercised | - | - | 676,060 | - | - | 676,060 |
| Net income for the period | - | - | - | 2,284,995 | - | 2,284,995 |
| Increase to reflect the present value of Redeemable non-controlling interest | - | - | - | (12,150) | - | (12,150) |
| Unrealized loss on foreign currency forward contracts treated as hedges | - | - | - | - | (38,046) | (38,046) |
| Reclassification to net income due to settlement of foreign currency forward contracts treated as hedges | - | - | - | - | 371,955 | 371,955 |

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Balance, June 30, 2015 11,083,976 \$14,411,616 \$22,492,630 \$(1,848,495) \$ (833,324) \$34,222,427

The following unaudited table summarizes stockholders' equity transactions for the six month period ended June 30, 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 | 187,653 | 830,343 | (282,888) | - | - | 547,455 |
| Repurchase and retirement of shares | (433,409) | (548,786) | (7,652,895) | - | - | (8,201,681) |
| Stock-based compensation | - | - | 249,653 | - | - | 249,653 |
| Income tax effect related to stock options exercised | - | - | 1,088,702 | - | - | 1,088,702 |
| Net income for the period | - | - | - | 5,118,938 | - | 5,118,938 |
| Increase to reflect the present value of Redeemable non-controlling interest | - | - | - | (12,150) | - | (12,150) |
| Unrealized loss on foreign currency forward contracts treated as hedges | - | - | - | - | (998,912) | (998,912) |
| Reclassification to net income due to settlement of foreign currency forward contracts treated as hedges | - | - | - | - | 788,029 | 788,029 |
| Balance, June 30, 2015 | 11,083,976 | \$14,411,616 | \$22,492,630 | \$(1,848,495) | \$ (833,324) | \$34,222,427 |

On January 8, 2015, the Company announced that it successfully concluded the 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 had 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 25,413 and 239,502 shares under this program during the three and six months ended June 30, 2015 for a total of \$489,536 and \$4,544,592, respectively.

On March 5, 2014, the Company announced a stock buyback program to 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 six months ended June 30, 2014 (none of which occurred during the quarter ended June 30, 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 June 30, 2015 and June 30, 2014 are as follows:

| Three months ended | | Three months ended | |
|---------------------------|-----------------|---------------------------|-----------------|
| June 30, 2015 | | June 30, 2014 | |
| Number | Weighted | Number | Weighted |
| of | Average | of | Average |
| Shares | | Shares | |

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| | | exercise price | | exercise price |
|------------------------------------|-----------|-----------------------|-----------|-----------------------|
| | | per share | | per share |
| Outstanding, beginning of period | 943,323 | \$ 6.23 | 1,107,257 | \$ 3.97 |
| Granted | — | — | — | — |
| Exercised | (112,656) | 2.66 | (48,108) | 2.72 |
| Forfeited | (1,716) | 13.15 | (6,091) | 5.71 |
| Expired | (1,875) | 2.40 | (750) | 3.20 |
| Outstanding, end of period | 827,076 | \$ 6.69 | 1,052,308 | \$ 4.01 |
| Options exercisable, end of period | 581,433 | \$ 4.58 | 824,641 | \$ 3.34 |

Details of stock option transactions for the six months ended June 30, 2015 and June 30, 2014 are as follows:

| | Six months ended | | Six months ended | |
|------------------------------------|-------------------------|---|-------------------------|---|
| | June 30, 2015 | | June 30, 2014 | |
| | Weighted | | Weighted | |
| | Number of Shares | Average exercise price per share | Number of Shares | Average exercise price per share |
| Outstanding, beginning of period | 976,062 | \$ 6.23 | 1,407,639 | \$ 3.80 |
| Granted | 45,000 | 19.41 | — | — |
| Exercised | (187,653) | 2.92 | (340,021) | 3.06 |
| Forfeited | (4,458) | 12.46 | (11,685) | 5.64 |
| Expired | (1,875) | 2.40 | (3,625) | 3.36 |
| Outstanding, end of period | 827,076 | \$ 6.69 | 1,052,308 | \$ 4.01 |
| Options exercisable, end of period | 581,433 | \$ 4.58 | 824,641 | \$ 3.34 |

As of June 30, 2015, the exercise prices, weighted average remaining contractual life and intrinsic values of outstanding options were as follows:

| Exercise price | Options outstanding | | | Aggregate intrinsic value | Options exercisable | | |
|-----------------------|----------------------------|--|--|----------------------------------|----------------------------|--|----------------------------------|
| | Outstanding Number | Weighted average exercise price per share | Weighted Average remaining contractual life | | Number exercisable | Weighted average exercise price per share | Aggregate intrinsic value |

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| | | | share | life (years) | | | share | | |
|---------|---|---------|--------------|---------------------|-----|--------------|--------------|----------|--------------|
| \$2.40 | - | \$2.92 | 358,111 | \$ 2.80 | 2.0 | \$8,969,483 | 334,192 | \$ 2.79 | \$8,373,182 |
| \$3.00 | - | \$5.76 | 210,875 | \$ 5.08 | 3.2 | 4,801,234 | 163,307 | \$ 4.95 | 3,739,827 |
| \$8.56 | - | \$10.16 | 116,815 | \$ 9.13 | 4.8 | 2,186,611 | 57,059 | \$ 8.94 | 1,078,921 |
| \$14.67 | - | \$19.41 | 141,275 | \$ 16.93 | 5.7 | 1,542,360 | 26,875 | \$ 15.37 | 335,313 |
| | | | 827,076 | \$ 6.69 | 3.4 | \$17,499,688 | 581,433 | \$ 4.58 | \$13,527,243 |

Total unrecognized compensation cost relating to unvested stock options at June 30, 2015, prior to the consideration of expected forfeitures, was approximately \$1,087,354 and is expected to be recognized over a weighted average period of 2.3 years.

The Company recorded stock-based compensation of \$124,605 and \$249,653 for the three and six months ended June 30, 2015 and \$85,357 and \$186,334 for the three and six months ended June 30, 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 June 30, 2015:

| | June 30, 2015 | | | |
|---------------------------------|--------------------|-------------|-------------|-------------|
| | Fair Value | | Liabilities | |
| | Measurements Using | | at | |
| | Level | Level | Level | Fair Value |
| | 1 | 2 | 3 | |
| Derivative instrument liability | \$— | \$1,523,647 | \$ — | \$1,523,647 |
| Total Liabilities | \$— | \$1,523,647 | \$ — | \$1,523,647 |

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 Measurements Using | | | Liabilities |
| | Level 1 | Level 2 | Level 3 | at |
| | | | | 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, as amended, or the Securities Act of 1933, as amended. 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 access the Internet (at home or on the go) or Internet services such as domain name registration, email and other Internet services. We are organized and managed based on two service offerings, Network Access Services and Domain 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, Network Access Services, which derives revenue from the sale of retail mobile phones and services as well as high speed Internet access, Internet hosting and network consulting services to individuals and small businesses, and Domain Services, which derives revenue from three distinct service offerings – Wholesale, Retail and Portfolio. 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 Network Access Services and Domain Services revenue separately.

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, LLC 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 113,000 subscribers and has over 178,000 devices under management.

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. 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 13.3 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 RealNames Service – based on over 36,000 surname domains – that allows roughly two-thirds of Americans to purchase an email address based on their last name.

Portfolio generates 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.

For the three months ended June 30, 2015 and June 30, 2014, we reported revenue of \$42.9 million and \$35.6 million, respectively. For the three months ended June 30, 2015 and June 30, 2014, our OpenSRS domain service offering accounted for 50% and 61% of our total revenue, respectively.

For the six months ended June 30, 2015 and June 30, 2014, we reported revenue of \$83.4 million and \$70.0 million, respectively. For the six months ended June 30, 2015 and June 30, 2014, our OpenSRS domain service offering accounted for 51% and 62% of our total revenue, respectively.

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. In addition to our results determined in accordance with GAAP, we believe the following non-GAAP measure is useful in evaluating our operating performance:

Adjusted EBITDA

Tucows reports all financial information required in accordance with United States generally accepted accounting principles (GAAP). Along with this information, to assist financial statement users in an assessment of our historical performance and to project our future earnings and cash flows, we typically disclose and discuss a non-GAAP financial measure, Adjusted EBITDA, on investor conference calls and related events that exclude non-cash and other charges as we believe that the non-GAAP information enhances investors' overall understanding of our financial performance and the comparability of our operating results from period to period.

The Company believes that the provision of this supplemental non-GAAP measure allows investors to evaluate the operational and financial performance of the Company's core business using the same evaluation measures that management uses. Adjusted EBITDA is one of the primary measures the Company uses for planning and budgeting purposes, incentive compensation and to monitor and evaluate our financial and operating results. Since adjusted EBITDA is a non-GAAP financial performance measure, our calculation of adjusted EBITDA may be susceptible to

varying calculations; may not be comparable to other similarly titled measures of other companies; and should not be considered in isolation, as a substitute for, or superior to measures of financial performance prepared in accordance with GAAP. Because Adjusted EBITDA is calculated before recurring cash charges, including interest expense and taxes, and is not adjusted for capital expenditures or other recurring cash requirements of the business, it should not be considered as a measure of discretionary cash available to invest in the growth of the business. See the Consolidated Statements of Cash Flows included in the attached financial statements. Non-GAAP financial measures do not reflect a comprehensive system of accounting, differ from GAAP measures with the same captions and may differ from non-GAAP financial measures with the same or similar captions that are used by other companies and/or analysts and may differ from period to period. However, the Company's management compensates for these limitations by providing the relevant disclosure of the items excluded in the calculation of adjusted EBITDA to net income based on U.S. GAAP, which should be considered when evaluating the Company's results. Tucows strongly encourages investors to review its financial information in its entirety and not to rely on a single financial measure.

Adjusted EBITDA excludes depreciation expense, amortization of intangibles, income tax provision, interest expense, interest income, stock-based compensation, asset impairment, net deferred revenue, which comprises the change in deferred revenue, net of prepaid domain name registry and other Internet services fees, to reflect the material amount of cash we collect and pay for domain registrations and other Internet services at the time of activation, unrealized foreign exchange gain/loss from the translation of monetary accounts denominated in non U.S. dollars to U.S. dollars as well as the revaluation of foreign exchange contracts and our foreign denominated assets and liabilities and infrequently occurring items.

The following table reconciles net income to adjusted EBITDA (dollars in thousands):

| | Three months ended June 30, | | Six months ended June 30, | |
|--|--------------------------------|----------|------------------------------|----------|
| | 2015 | 2014 | 2015 | 2014 |
| | (unaudited) | | (unaudited) | |
| Net income for the period | \$2,285 | \$ 1,347 | \$5,119 | \$ 1,824 |
| Depreciation of property and equipment | 342 | 227 | 601 | 466 |
| Amortization of intangible assets | 106 | 545 | 176 | 1,015 |
| Interest expense, net | 57 | 69 | 82 | 143 |
| Provision for income taxes | 1,540 | 666 | 3,092 | 918 |
| Change in net deferred revenue (1) | 200 | 266 | 891 | 1,198 |
| Stock-based compensation | 125 | 85 | 250 | 186 |
| Loss on currency forward contracts | 702 | 70 | 2,039 | 839 |
| Adjusted EBITDA | \$5,357 | \$ 3,275 | \$12,250 | \$ 6,589 |

Net deferred revenue comprises the change in deferred revenue, net of prepaid domain name registry and other Internet services fees, to reflect the material amount of cash we collect and pay for domain registrations and other Internet services at the time of activation. Net deferred revenue for the three and six months ended June 30, 2015, includes a benefit of \$0.1 million as a result of the translation of deferred revenue and prepaid domain name registry and other Internet services fees to our reporting currency of US dollars.

Adjusted EBITDA increased to \$5.4 million and \$12.3 million in the three and six months ended June 30, 2015 from \$3.3 million and \$6.6 million in the three and six months ended June 30, 2014, respectively. The increase in adjusted EBITDA from period to period was primarily driven by the growth in Ting mobile services.

Domain Services

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

| | Three months ended | | Six months ended | |
|---|---------------------------|-------------|-------------------------|-------------|
| | June 30, 2015 | 2014 | June 30, 2015 | 2014 |
| | (1) | (1) | (1) | (1) |
| | (in 000's) | | (in 000's) | |
| Total new, renewed and transferred-in domain name registrations | 2,423 | 2,386 | 4,878 | 4,814 |

(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:

| | June 30, | |
|--|-------------------|-------------|
| | 2015 | 2014 |
| | (1) | (1) |
| | (in 000's) | |
| Domain names under management: | | |
| Registered using the Tucows Registrar Accreditation | 10,228 | 10,365 |
| Registered using our Resellers' Registrar Accreditations | 3,023 | 3,204 |
| Total domain names under management | 13,251 | 13,569 |

(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

June 30,
2015 (1) 2014 (1)

| | | |
|-----------------------------------|---------|---------|
| Ting subscribers under management | 113,000 | 73,000 |
| Ting devices under management | 178,000 | 113,000 |

(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

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.

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.

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

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, LLC on February 27, 2015, we began providing high speed Internet access, Internet hosting and network consulting to customers in Central Virginia.

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”).

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.

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 AND SIX MONTHS ENDED JUNE 30, 2015 AS COMPARED TO THE THREE AND SIX MONTHS ENDED JUNE 30, 2014

NET REVENUES

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

| | Three months ended June 30, | | Six months ended June 30, | |
|--|------------------------------------|--------------|----------------------------------|--------------|
| | 2015 | 2014 | 2015 | 2014 |
| <u>Domain Services:</u> | | | | |
| Wholesale | | | | |
| Domain Services | \$21,286,863 | \$21,503,086 | \$42,461,994 | \$43,152,040 |
| Value Added Services | 2,355,837 | 2,395,726 | 4,597,835 | 4,999,331 |
| Total Wholesale | 23,642,700 | 23,898,812 | 47,059,829 | 48,151,371 |
| Retail | 3,009,465 | 2,540,538 | 5,885,193 | 4,924,601 |
| Portfolio | 819,086 | 888,806 | 2,067,048 | 1,942,446 |
| Total Domain Services | 27,471,251 | 27,328,156 | 55,012,070 | 55,018,418 |
| <u>Network Access Services:</u> | | | | |
| Ting | 15,417,969 | 8,259,845 | 28,344,983 | 14,971,977 |
| Total Network Access Services | 15,417,969 | 8,259,845 | 28,344,983 | 14,971,977 |
| | \$42,889,220 | \$35,588,001 | \$83,357,053 | \$69,990,395 |
| Increase over prior period | \$7,301,219 | | \$13,366,658 | |
| Increase - percentage | 21 | % | 19 | % |

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

| | Three months ended June 30, | | Six months ended June 30, | |
|--------------------------------|------------------------------------|-------------|----------------------------------|-------------|
| | 2015 | 2014 | 2015 | 2014 |
| <u>Domain Services:</u> | | | | |
| Wholesale | | | | |
| Domain Services | 50 % | 61 % | 51 % | 62 % |
| Value Added Services | 5 % | 7 % | 6 % | 7 % |

| | | | | |
|-----------------------|------|------|------|------|
| Total Wholesale | 55 % | 68 % | 57 % | 69 % |
| Retail | 7 % | 7 % | 7 % | 7 % |
| Portfolio | 2 % | 2 % | 2 % | 3 % |
| Total Domain Services | 64 % | 77 % | 66 % | 79 % |

Network Access Services:

| | | | | |
|-------------------------------|-------|-------|-------|-------|
| Ting | 36 % | 23 % | 34 % | 21 % |
| Total Network Access Services | 36 % | 23 % | 34 % | 21 % |
| | 100 % | 100 % | 100 % | 100 % |

Total net revenues for the three months ended June 30, 2015 increased by \$7.3 million or 21% to \$42.9 million when compared to the three months ended June 30, 2014.

Total net revenues for the six months ended June 30, 2015 increased by \$13.4 million or 19% to \$83.4 million when compared to the six months ended June 30, 2014.

Deferred revenue increased to \$74.3 million at June 30, 2015 from \$73.6 million at June 30, 2014.

No customer accounted for more than 10% of revenue during the three and six months ended June 30, 2015 and June 30, 2014. At June 30, 2015 two customers accounted for 21% of accounts receivable. At June 30, 2014, one customer accounted for 12% 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 June 30, 2015, domain services revenue decreased by \$0.2 million to \$21.3 million when compared to the three months ended June 30, 2014. During the six months ended June 30, 2015, domain services revenue decreased by \$0.7 million to \$42.5 million when compared to the six months ended June 30, 2014.

During the three months ended June 30, 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 June 30, 2014. During the six months ended June 30, 2015, the number of transactions from all new, renewed and transferred-in domain name registrations that we processed increased by 0.1 million to 4.9 million when compared to the six months ended June 30, 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 June 30, 2015, total domains that we manage under our own accreditation decreased to 10.2 million when compared to 10.4 million at June 30, 2014. These decreases in domains under management primarily resulted from the same factors impacting domain transactions mentioned above. Also, as of June 30, 2015, total domains that we manage on behalf of other accredited registrars decreased to 3.0 million when compared to 3.2 million at the end of June 30, 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 June 30, 2015, value added services revenue remained relatively flat at \$2.4 million when compared to the three months ended June 30, 2014. During the six months ended June 30, 2015, value added services revenue decreased by \$0.4 million to \$4.6 million when compared to the six months ended June 30, 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 June 30, 2015, as compared to the three months ended June 30, 2014, increased by \$0.5 million, or 18%, to \$3.0 million. Net revenues from Retail for the six months ended June 30, 2015, as compared to the six months ended June 30, 2014, increased by \$1.0 million, or 20%, to \$5.9 million. These increases were 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.

Portfolio

Net revenues from Portfolio for the three months ended June 30, 2015, as compared to the three months ended June 30, 2014, decreased by \$0.1 million to \$0.8 million. This decrease primarily related to lower sales of online

advertising.

Net revenues from Portfolio for the six months ended June 30, 2015, as compared to the six months ended June 30, 2014, increased by \$0.1 million to \$2.1 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 and a decrease in online advertising revenue.

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 equipment and services and the provisioning of high speed Internet access, Internet hosting and network consulting services for the three months ended June 30, 2015, as compared to the three months ended June 30, 2014, increased by \$7.2 million or 87% to \$15.4 million primarily reflecting the impact the larger Ting subscriber base is having on revenue. Network access services revenue were also impacted by our generating \$1.1 million in provisioning of high speed Internet access, Internet hosting and network consulting services during the three months ended June 30, 2015 when compared to the three months ended June 30, 2014. Net revenues from Ting mobile phone equipment and services and the provisioning of high speed Internet access, Internet hosting and network consulting services for the six months ended June 30, 2015, as compared to the six months ended June 30, 2014, increased by \$13.4 million or 89% to \$28.3 million. This increase primarily reflects the impact the larger subscriber base is having on service revenues. As of June 30, 2015, Ting had 113,000 subscribers and 178,000 mobile devices under its management compared to 73,000 subscribers and 113,000 devices under management as of June 30, 2014.

COST OF REVENUES

Network Access Services

The costs of revenue for Ting's mobile phone equipment and services 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 MNOs. Costs for the provisioning of high speed Internet access, Internet hosting and network consulting services include costs for network access fees and software licenses.

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.

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 June 30, | | Six months ended June 30, | |
|--|------------------------------------|--------------|----------------------------------|--------------|
| | 2015 | 2014 | 2015 | 2014 |
| <u>Domain Services:</u> | | | | |
| Wholesale | | | | |
| Domain Services | \$17,749,516 | \$17,809,325 | \$35,297,543 | \$36,044,540 |
| Value Added Services | 501,518 | 563,011 | 1,037,650 | 1,103,733 |
| Total Wholesale | 18,251,034 | 18,372,336 | 36,335,193 | 37,148,273 |
| Retail | 1,322,620 | 1,110,659 | 2,543,120 | 2,126,075 |
| Portfolio | 178,381 | 213,035 | 349,939 | 456,890 |
| Total Domain Services | 19,752,035 | 19,696,030 | 39,228,252 | 39,731,238 |
| <u>Network Access Services:</u> | | | | |
| Ting | 8,498,637 | 5,039,974 | 15,843,794 | 9,321,405 |
| Total Network Access Services | 8,498,637 | 5,039,974 | 15,843,794 | 9,321,405 |
| <u>Network Expenses:</u> | | | | |
| Network, other costs | 1,494,838 | 1,144,697 | 2,716,934 | 2,288,341 |
| Network, depreciation and amortization costs | 291,461 | 173,963 | 495,027 | 356,937 |
| Total Network Expenses | 1,786,299 | 1,318,660 | 3,211,961 | 2,645,278 |
| | \$30,036,971 | \$26,054,664 | \$58,284,007 | \$51,697,921 |
| Increase over prior period | \$3,982,307 | | \$6,586,086 | |
| Increase - percentage | 15 | % | 13 | % |

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

| | Three months ended June 30, | | Six months ended June 30, | |
|--------------------------------|------------------------------------|-------------|----------------------------------|-------------|
| | 2015 | 2014 | 2015 | 2014 |
| <u>Domain Services:</u> | | | | |
| Wholesale | | | | |
| Domain Services | 41 % | 50 % | 42 % | 51 % |
| Value Added Services | 1 % | 2 % | 1 % | 2 % |
| Total Wholesale | 42 % | 52 % | 43 % | 53 % |
| Retail | 3 % | 3 % | 3 % | 3 % |
| Portfolio | 1 % | 1 % | 1 % | 1 % |

| | | | | |
|--|-----|------|-----|------|
| Total Domain Services | 46% | 56 % | 47% | 57 % |
| <u>Network Access Services:</u> | | | | |
| Ting | 20% | 14 % | 19% | 13 % |
| Total Network Access Services | 20% | 14 % | 19% | 13 % |
| <u>Network Expenses:</u> | | | | |
| Network, other costs | 3 % | 3 % | 3 % | 3 % |
| Network, depreciation and amortization costs | 1 % | 0 % | 1 % | 1 % |
| Total Network Expenses | 4 % | 3 % | 4 % | 4 % |
| | 70% | 73 % | 70% | 74 % |

Total cost of revenues for the three months ended June 30, 2015 increased by \$4.0 million, or 15%, to \$30.0 million when compared to the three months ended June 30, 2014. Total cost of revenues for the six months ended June 30, 2015 increased by \$6.6 million, or 13%, to \$58.3 million when compared to the six months ended June 30, 2014. This increase primarily resulted from the impact Ting's larger subscriber base has on network access service costs.

Prepaid domain registration and other Internet services fees as of June 30, 2015 increased to \$58.6 million from \$58.5 million as of June 30, 2014.

Wholesale

Costs for Wholesale for the three months ended June 30, 2015 remained relatively flat at \$18.3 million when compared to the three months ended June 30, 2014. Costs for Wholesale for the six months ended June 30, 2015 decreased by \$0.8 million, or 2%, to \$36.3 million when compared to the six months ended June 30, 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 June 30, 2015 increased by \$0.2 million, to \$1.3 million when compared to the three months ended June 30, 2014. Costs for Retail for the six months ended June 30, 2015 increased by \$0.4 million, to \$2.5 million when compared to the six months ended June 30, 2014. These increases resulted primarily from the increased cost of additional volume in Hover services.

Portfolio

Costs for Portfolio for the three months ended June 30, 2015 remained relatively flat at \$0.2 million when compared to the three months ended June 30, 2014. Costs for Portfolio for the six months ended June 30, 2015 decreased by \$0.1 million, to \$0.3 million when compared to the six months ended June 30, 2014. This resulted from our decision not to renew certain domain names acquired in the June 2006 acquisition of Mailbank.com Inc. as described under impairment of indefinite life intangible assets below.

Network Access Services

Costs for Network Access Services for the three months ended June 30, 2015 increased by \$3.5 million, to \$8.5 million when compared to the three months ended June 30, 2014 and primarily reflects the impact the larger Ting subscriber base is having on service costs. Cost of network access services were also impacted by our incurring \$0.6 million in the provisioning of high speed Internet access, Internet hosting and network consulting services costs during the three months ended June 30, 2015 when compared to the three months ended June 30, 2014. Costs for Network Access Services for the six months ended June 30, 2015 increased by \$6.5 million, to \$15.8 million when compared to the six months ended June 30, 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 June 30, 2015 increased by \$0.4 million, to \$1.5 million when compared to the three months ended June 30, 2014. Network costs before depreciation and amortization for the six months ended June 30, 2015 increased by \$0.4 million, to \$2.7 million when compared to the six months ended June 30, 2014. This increase is primarily the result of the additional costs we incurred as a result of our providing high speed Internet access, Internet hosting and network consulting to customers.

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 | | Six months ended June | | | |
|----------------------------|---------------------------|-------------|------------------------------|-------------|----|---|
| | June 30, | | 30, | | | |
| | 2015 | 2014 | 2015 | 2014 | | |
| Sales and marketing | \$4,847,963 | \$3,762,441 | \$8,647,138 | \$7,784,215 | | |
| Increase over prior period | \$1,085,522 | | \$862,923 | | | |
| Increase - percentage | 29 | % | 11 | % | | |
| Percentage of net revenues | 11 | % | 11 | % | 10 | % |

Sales and marketing expenses for the three months ended June 30, 2015 increased by \$1.1 million, or 29%, to \$4.8 million when compared to the three months ended June 30, 2014. This increase related primarily to an increase in workforce related expenses of \$0.9 million and an increase of \$0.2 million in marketing spend largely to support and acquire Ting subscribers.

Sales and marketing expenses for the six months ended June 30, 2015 increased by \$0.9 million, or 11%, to \$8.6 million when compared to the six months ended June 30, 2014. This increase related primarily to increased workforce related expenses of \$1.1 million which was partially offset by a lower marketing spend of \$0.2 million, primarily the result of our decision last year to experiment with broader advertising initiatives as a means of accelerating our brand awareness and consideration.

As we expect to exceed the adjusted EBITDA target set for Fiscal 2015 under our overachievement bonus program, sales and marketing workforce related costs in both the three and six months ended June 30, 2015, include a provision of \$0.4 million due to this higher performance attainment.

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 | | Six months ended June | | | |
|--------------------------------------|---------------------------|-------------|------------------------------|-------------|---|---|
| | June 30, | | 30, | | | |
| | 2015 | 2014 | 2015 | 2014 | | |
| Technical operations and development | \$1,189,276 | \$1,107,532 | \$2,303,471 | \$2,197,430 | | |
| Increase over prior period | \$81,744 | | \$106,041 | | | |
| Increase - percentage | 7 | % | 5 | % | | |
| Percentage of net revenues | 3 | % | 3 | % | 3 | % |

Technical operations and development expenses for the three and six months ended June 30, 2015 increased slightly to \$1.2 million and \$2.3 million, respectively when compared to the three and six months ended June 30, 2014. As we expect to exceed the adjusted EBITDA target set for Fiscal 2015 under our overachievement bonus program, technical operations workforce related costs in both the three and six months ended June 30, 2015, include a provision of \$0.1 million due to this higher performance attainment.

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 | | Six months ended June | | | |
|----------------------------|---------------------------|-------------|------------------------------|-------------|---|---|
| | June 30, | | 30, | | | |
| | 2015 | 2014 | 2015 | 2014 | | |
| General and administrative | \$2,173,254 | \$1,886,319 | \$3,988,442 | \$3,654,119 | | |
| Increase over prior period | \$286,935 | | \$334,323 | | | |
| Increase - percentage | 15 | % | 9 | % | | |
| Percentage of net revenues | 5 | % | 5 | % | 5 | % |

General and administrative expenses for the three months ended June 30, 2015 increased by \$0.3 million, or 15%, to \$2.2 million when compared to the three months ended June 30, 2014. As we expect to exceed the adjusted EBITDA target set for Fiscal 2015 under our overachievement bonus program, general and administrative workforce related costs in both the three and six months ended June 30, 2015, include a provision of \$0.4 million due to this higher performance attainment. In addition, credit card processing fees, facility costs and supplies increased by \$0.2 million when compared to the three months ended June 30, 2014 primarily to support the growth of Ting. These increases were partially offset by our recognizing, during the three months ended June 30, 2015, a gain on realized foreign exchange of \$0.7 million compared to a gain of \$0.2 million during the three months ended June 30, 2014. These gains in turn were partially offset by our incurring a loss on foreign exchange revaluation of our foreign denominated assets and liabilities of \$0.1 million during the three months ended June 30, 2015 compared to a gain of \$26,000 during the three months ended June 30, 2014.

General and administrative expenses for the six months ended June 30, 2015 increased by \$0.3 million, or 9%, to \$4.0 million when compared to the six months ended June 30, 2014. This increase was primarily the result of increased people costs of \$0.3 million, credit card processing fees, facility costs and supplies increase of \$0.4 million when compared to the six months ended June 30, 2014 primarily to support the growth of Ting. These increases were partially offset by our recognizing, during the six months ended June 30, 2015, a gain on realized foreign exchange of \$1.5 million compared to a gain of \$0.7 million during the three months ended June 30, 2014. These gains in turn were partially offset by our incurring a loss on foreign exchange revaluation of our foreign denominated assets and liabilities of \$0.5 million during the six months ended June 30, 2015 compared to a loss of \$0.2 million during the six months ended June 30, 2014.

DEPRECIATION OF PROPERTY AND EQUIPMENT

| | Three months ended June 30, | | Six months ended June 30, | | | |
|--|-----------------------------|----------|---------------------------|-----------|---|---|
| | 2015 | 2014 | 2015 | 2014 | | |
| Depreciation of property and equipment | \$62,022 | \$52,538 | \$121,284 | \$108,842 | | |
| Increase over prior period | \$9,484 | | \$12,442 | | | |
| Increase - percentage | 18 | % | 11 | % | | |
| Percentage of net revenues | 0 | % | 0 | % | 0 | % |

Depreciation costs remained relatively flat at \$0.1 million and \$0.1 million for the three and six months ended June 30, 2015 and June 30, 2014, respectively.

AMORTIZATION OF INTANGIBLE ASSETS

| | Three months ended June 30, | | Six months ended June 30, | | | |
|---------------------------------------|-----------------------------|-----------|---------------------------|-----------|---|---|
| | 2015 | 2014 | 2015 | 2014 | | |
| Amortization of intangible assets | \$56,997 | \$219,030 | \$110,212 | \$438,060 | | |
| (Decrease) increase over prior period | \$(162,033) | | \$(327,848) | | | |
| Decrease - percentage | (74) |)% | (75) |)% | | |
| Percentage of net revenues | 0 | % | 1 | % | 0 | % |

Amortization of intangible assets for the three and six months ended June 30, 2015, consists of amounts arising in connection with the acquisition of the acquisition of EPAG Domainservices GmbH ("EPAG") in July 2011 and the acquisition of the BRI Group in February 2015. Amortization for the three and six months ended June 30, 2014 also included the remaining amortization arising in connection with the acquisition of ItsYourDomain.com ("IYD") in July 2007.

Network rights, brand and customer relationships acquired in connection with the acquisitions of IYD, EPAG and the BRI Group are amortized on a straight-line basis over seven years.

IMPAIRMENT OF INDEFINITE LIFE INTANGIBLE ASSETS

| | Three months ended June 30, | | Six months ended June 30, | | |
|---|--------------------------------|-----------|------------------------------|-----------|---|
| | 2015 | 2014 | 2015 | 2014 | |
| Impairment of indefinite life intangible assets | \$37,805 | \$326,457 | \$50,298 | \$577,145 | |
| Decrease over prior period | \$(288,652) | | \$(526,847) | | |
| Decrease - percentage | (88 |)% | (91 |)% | |
| Percentage of net revenues | 0 | % 1 | % 0 | % 1 | % |

As part of our normal renewal process during the three and six months ended June 30, 2015, we assessed that certain domain names acquired in the June 2006 acquisition of Mailbank.com Inc. should not be renewed and were allowed to expire. Accordingly, these domain names, with a book value of \$37,805 and \$50,298 respectively, have been written off and recorded as impairment of indefinite life intangible assets. During the three and six months ended June 30, 2014 we assessed that domain names with a book value of \$0.3 million and \$0.6 million should not be renewed and were allowed to expire.

LOSS ON CURRENCY FORWARD CONTRACTS

Although our functional currency is the U.S. dollar, a major portion of our fixed expenses are incurred in Canadian dollars. Our goal with regard to foreign currency exposure is, to the extent possible, to achieve operational cost certainty, manage financial exposure to certain foreign exchange fluctuations and to neutralize some of the impact of foreign currency exchange movements. Accordingly, we enter into foreign exchange contracts to mitigate the exchange rate risk on portions of our Canadian dollar exposure.

| | Three months ended June 30, | | Six months ended June 30, | | |
|------------------------------------|--------------------------------|----------|------------------------------|-----------|---|
| | 2015 | 2014 | 2015 | 2014 | |
| Loss on currency forward contracts | \$602,439 | \$96,545 | \$1,559,297 | \$647,916 | |
| Increase over prior period | \$505,894 | | \$911,381 | | |
| Increase - percentage | 524 | % | 141 | % | |
| Percentage of net revenues | 1 | % 0 | % 2 | % 1 | % |

As of June 30, 2015, we have entered into certain forward exchange contracts that do not comply with the requirements of hedge accounting to meet a portion of our future Canadian dollar requirements through October 2016. The impact of the fair value adjustment on outstanding contracts for the three months ended June 30, 2015 was a net gain of \$0.1 million, compared to a net gain of \$0.2 million for the three months ended June 30, 2014. In addition, the impact of the fair value adjustment on outstanding contracts was increased by a realized loss upon settlement of currency forward contracts of \$0.7 million for the three months ended June 30, 2015, compared to a net loss of \$0.3 million during the three months ended June 30, 2014.

The impact of the fair value adjustment on outstanding contracts for the six months ended June 30, 2015 was a net loss of \$0.1 million, compared to a net gain of \$0.1 million for the three months ended June 30, 2014. In addition, the impact of the fair value adjustment on outstanding contracts was increased by a realized loss upon settlement of currency forward contracts of \$1.5 million for the six months ended June 30, 2015, compared to a net loss of \$0.8 million during the six months ended June 30, 2014.

At June 30, 2015, our balance sheet reflects a net derivative instrument liability of \$1.5 million as a result of our existing foreign exchange contracts.

OTHER INCOME AND EXPENSES

| | Three months ended | | Six months ended | |
|-----------------------------|---------------------------|-------------|-------------------------|-------------|
| | June 30, | | June 30, | |
| | 2015 | 2014 | 2015 | 2014 |
| Other income (expense), net | \$(57,402) | \$(69,348) | \$(82,177) | \$(143,181) |
| Decrease over prior period | \$11,946 | | \$61,004 | |
| Decrease - percentage | (17)% | | (43)% | |
| Percentage of net revenues | 0 % | 0 % | 0 % | 0 % |

Other expenses for the three and six months ended June 30, 2015 decreased to \$0.1 million and \$0.1 million respectively when compared to the three and six months ended June 30, 2014 and primarily consist of interest we incur in connection with our credit facility with the Bank of Montreal (as discussed below).

INCOME TAXES

| | Three months ended | | Six months ended June | | | | | |
|---|---------------------------|-------------|------------------------------|-------------|---|---|---|---|
| | June 30, | | 30, | | | | | |
| | 2015 | 2014 | 2015 | 2014 | | | | |
| Provision for income taxes | \$1,540,096 | \$665,945 | \$3,091,789 | \$917,545 | | | | |
| Increase in provision over prior period | \$874,151 | | \$2,174,244 | | | | | |
| Increase - percentage | 131 | % | 237 | % | | | | |
| Percentage of net revenues | 4 | % | 2 | % | 4 | % | 1 | % |

For the three months ended June 30, 2015, we recorded a provision for income taxes of \$1.5 million on income before income taxes of \$3.8 million, using an estimated effective tax rate for Fiscal 2015 adjusted for certain minimum state taxes. Comparatively, for the three months ended June 30, 2014, we recorded a provision for income taxes of \$0.7 million on income before taxes of \$2.0 million, using an estimated effective tax rate for the 2014 fiscal year.

For the six months ended June 30, 2015, we recorded a provision for income taxes of \$3.0 million on income before income taxes of \$8.2 million, using an estimated effective tax rate for Fiscal 2015 adjusted for certain minimum state taxes. Comparatively, for the six months ended June 30, 2014, we recorded a provision for income taxes of \$0.9 million on income before taxes of \$2.7 million, using an estimated effective tax rate for the 2014 fiscal year.

In assessing the realizability of deferred tax assets, we consider 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. We consider projected future taxable income, uncertainties related to the industry in which we operate, and tax planning strategies in making this assessment.

We follow 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.

We had approximately \$0.1 million of total gross unrecognized tax benefit as of June 30, 2015 and as of December 31, 2014, which if recognized would favorably affect our income tax rate in future periods. The unrecognized tax benefit relates primarily to prior year Pennsylvania state franchise taxes. We recognize accrued interest and penalties related to income taxes in income tax expense. We did not have significant interest and penalties accrued at June 30, 2015 and December 31, 2014, respectively.

OTHER COMPREHENSIVE INCOME (LOSS)

To mitigate the impact of the change in fair value of our foreign exchange contracts on our financial results, in October 2012 we began applying hedge accounting for the majority of the contracts we need to meet our Canadian dollar requirements on a prospective basis.

The impact of the fair value adjustment on outstanding hedged contracts for the three and six months ended June 30, 2015 was a net gain in other comprehensive income of \$0.3 million and a net loss in other comprehensive income of \$0.2 million respectively. The impact of the fair value adjustment on outstanding hedged contracts for the three and six months ended June 30, 2014 was a net gain in other comprehensive income of \$0.4 million and \$0.2 million respectively.

The following table presents other comprehensive income for the periods presented:

| | Three months ended | | Six months ended | |
|---|---------------------------|-------------|-------------------------|-------------|
| | June 30, | | June 30, | |
| | 2015 | 2014 | 2015 | 2014 |
| Comprehensive income (loss) | \$333,909 | \$430,277 | \$(210,883) | \$214,810 |
| Decrease in provision over prior period | \$(96,368) | | \$(425,693) | |
| Decrease - percentage | (22 |)% | (198 |)% |
| Percentage of net revenues | 1 | % | 1 | % |
| | (0 |)% | 0 | % |

LIQUIDITY AND CAPITAL RESOURCES

As of June 30, 2015, our cash and cash equivalents balance increased by \$7.0 million to \$15.3 million when compared to December 31, 2014. Our principal sources of liquidity during the six months ended June 30, 2015 resulted from cash provided by operating activities of \$5.2 million, the proceeds of \$6.6 million we received on our previously announced agreement to amend our .online joint venture relationship to a marketing agreement, the proceeds of \$3.5 million we received under our Amended Credit Facility to fund the previously announced acquisition of a controlling interest in Ting Virginia, LLC and the exercise of stock options of \$1.6 million. The resulting proceeds from the exercise of stock options of \$1.6 million include an excess tax benefit from share based compensation expenses of \$1.1 million. These sources of funds were partly offset by our repurchasing 239,502 of our shares for \$4.5 million through our open market stock buyback that commenced on February 16, 2015, our repurchasing 193,907 shares for \$3.7 million through our modified Dutch Auction tender offer (the “Tender Offer”) that closed on January 7, 2015 and our investing \$1.3 million in additions to property and equipment.

We have credit agreements (collectively the “Amended Credit Facility”) with the Bank of Montreal which provide us with access to a demand loan revolving facility (the “2012 DLR Loan”) and a demand loan revolving reducing facility (the “2012 DLRR Loan”) that provide for a \$14 million, five-year revolving credit facility, a \$3.5 million treasury risk management facility and a \$1.0 million operating demand loan. At June 30, 2015 the balance under the 2012 DLRR Loan was \$3.5 million and the 2012 DLR Loan was fully repaid. Both of these financing arrangements remain available to fund future operations of the Company, with no set expiration date.

In accordance with the terms of the demand loan facilities, repayment of advances under the 2012 DLR Loan consist of interest only payments at U.S. Base Rate plus 1.25%, made monthly in arrears, and prepayment is permitted without penalty.

The Amended Credit Facility also provides for a \$3.5 million settlement risk line to assist us with hedging Canadian dollar exposure through foreign exchange forward contracts and/or currency options. Under the terms of the Amended Credit Facility, we may enter into such agreements at market rates with terms not to exceed 18 months. As of June 30, 2015, we held contracts in the amount of \$24.0 million to trade U.S. dollars in exchange for Canadian dollars.

The Amended Credit Facility contains customary events of default and affirmative and negative covenants and restrictions, including certain financial maintenance covenants such as a maximum total funded debt to EBITDA ratio and a minimum fixed charge ratio. As of June 30, 2015, we were in compliance with all our covenants.

Cash Flow from Operating Activities

Net cash provided by operating activities during the six months ended June 30, 2015 was \$5.2 million, as compared to \$1.1 million during the six months ended June 30, 2014.

Net income, after adjusting for non-cash charges, during the six months ended June 30, 2015 was \$5.3 million. Net income included non-cash charges and recoveries of \$0.1 million such as depreciation, amortization, impairment of indefinite life intangible asset, stock-based compensation, the provision for unrealized losses on currency forward contracts, excess tax benefit related to stock-based compensation and a recovery for deferred tax. In addition, changes in our working capital used \$0.1 million. Positive contributions of \$5.4 million from movements in deferred revenue, income taxes, accounts payable, accrued liabilities, customer deposits and accreditation fees payable were offset by our utilizing \$5.5 million to fund a increases in deferred registration costs, prepaid expenses and deposits, accounts receivable and inventory.

Cash Flow from Financing Activities

Net cash outflows from financing activities during the six months ended June 30, 2015 totaled \$3.1 million as compared to our generating \$1.0 million during the six months ended June 30, 2014. Net cash outflows amounting to \$8.2 million resulted from \$4.5 million used to fund our repurchasing 239,502 of our shares during the six months through our open market stock buyback that commenced on February 16, 2015 and our repurchasing of 193,907 shares for \$3.7 million through our Tender Offer that closed on January 7, 2015. These cash outflows were partially offset by cash inflows of \$3.5 million we received under our Amended Credit Facility to fund the previously announced acquisition of a controlling interest in Ting Virginia, LLC and the exercise of stock options of \$1.6 million. The resulting proceeds from the exercise of stock options of \$1.6 million includes an excess tax benefit from share based compensation expenses of \$1.1 million.

Cash Flow from Investing Activities

Investing activities during the six months ended June 30, 2015 generated net cash of \$4.9 million as compared to our use of \$0.4 million during the six months ended June 30, 2014.

Investing activities benefited from the proceeds of \$6.6 million we received on our previously announced agreement with our .online joint venture partners to release each other from any and all obligations under the .online joint venture Term Sheet and instead enter into a Joint Marketing Agreement to launch marketing programs, with incentives and obligations to ensure the success of the .online registry. These marketing arrangements will contribute \$1.5 million, which will be recognized evenly over the term of the marketing agreement once .online is generally available.

On February 27, 2015, Ting Fiber, Inc., one of our wholly owned subsidiaries, acquired a controlling 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. 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. In addition, we used \$1.3 million to acquire additional property and equipment. Included in these additions is an amount of \$0.9 million that we have invested since the acquisition of the BRI Group primarily in expanding our fiber footprint.

Based on our operations, we believe that our cash flow from operations will be adequate to meet our anticipated requirements for working capital, capital expenditures and our loan repayments for at least the next 12 months.

We may choose to raise additional funds or seek other financing arrangements to facilitate more rapid expansion, develop new or enhance existing products or services, respond to competitive pressures or acquire or invest in complementary businesses, technologies, services or products.

If additional financing is required, we may not be able to raise it on acceptable terms, or at all, and additional financing may be dilutive to existing investors. We may also evaluate potential acquisitions of other businesses, products and technologies. To complete potential acquisitions, we may issue additional securities or need additional equity or debt financing and any additional financing may be dilutive to existing investors. There are currently no material understandings, commitments or agreements regarding the acquisition of other businesses.

Off-Balance Sheet Arrangements

As of June 30, 2015, we did not have any off-balance sheet arrangements, as defined in Item 303(a)(4)(ii) of SEC Regulation S-K.

Contractual Obligations

In our Annual Report on Form 10-K for the year ended December 31, 2014, we disclosed our contractual obligations.

The Company has entered into a network management agreement with the City of Westminster, Maryland (“the City”) to run and operate their fiber optic network for a period of 10 years. Under the terms of this agreement, the Company is obligated to making certain minimum performance commitments. In addition, should certain minimum performance criteria not be met, the Company would be liable to contribute up to \$100,000 per quarter towards the City’s debt service costs.

As of June 30, 2015, there have been no other material changes to those contractual obligations outside the ordinary course of business.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

We develop products in Canada and sell these services in North America and Europe. Our sales are primarily made in U.S. dollars, while a major portion of expenses are incurred in Canadian dollars. Our financial results could be affected by factors such as changes in foreign currency exchange rates or weak economic conditions in foreign markets. Our interest income is sensitive to changes in the general level of Canadian and U.S. interest rates, particularly since the majority of our investments are in short-term instruments. Based on the nature of our short-term investments, we have concluded that there is no material interest rate risk exposure as of June 30, 2015. We are also subject to market risk exposure related to changes in interest rates under our Amended Credit Facility. We do not expect that any changes in interest rates will be material; however, fluctuations in interest rates are beyond our control. We will continue to monitor and assess the risks associated with interest expense exposure and may take additional actions in the future to mitigate these risks.

Although our functional currency is the U.S. dollar, a substantial portion of our fixed expenses are incurred in Canadian dollars. Our policy with respect to foreign currency exposure is to manage financial exposure to certain foreign exchange fluctuations with the objective of neutralizing some of the impact of foreign currency exchange movements. Exchange rates are, however, subject to significant and rapid fluctuations, and therefore we cannot predict the prospective impact of exchange rate fluctuations on our business, results of operations and financial condition. Accordingly, we have entered into foreign exchange contracts to mitigate the exchange rate risk on portions of our Canadian dollar exposure.

At June 30, 2015, we had the following outstanding forward exchange contracts to trade U.S. dollars in exchange for Canadian dollars:

| Maturity date | Notional amount of U.S. dollars | Weighted average exchange rate of U.S. dollars | Fair value |
|--------------------------|---------------------------------|--|---------------|
| July – September, 2015 | \$6,500,000 | 1.1282 | \$(632,049) |
| October – December, 2015 | 6,542,500 | 1.1539 | (507,619) |
| January – March, 2016 | 3,407,500 | 1.2075 | (120,238) |
| April – June, 2016 | 3,257,500 | 1.2080 | (114,296) |
| July – September, 2016 | 3,257,500 | 1.2079 | (113,274) |
| October 2016 | 1,052,500 | 1.2079 | (36,171) |
| Total | \$24,017,500 | 1.1716 | \$(1,523,647) |

As of June 30, 2015, we had \$24.0 million of outstanding foreign exchange forward contracts which will convert to CDN \$28.1 million. Of these contracts, \$20.4 million met the requirements for hedge accounting (June 30, 2014 - \$13.5 million of which \$10.5 million were designated as hedges).

We have performed a sensitivity analysis model for foreign exchange exposure over the three months ended June 30, 2015. The analysis used a modeling technique that compares the U.S. dollar equivalent of all expenses incurred in Canadian dollars, at the actual exchange rate, to a hypothetical 10% adverse movement in the foreign currency exchange rates against the U.S. dollar, with all other variables held constant. Foreign currency exchange rates used were based on the market rates in effect during the three months ended June 30, 2015. The sensitivity analysis indicated that a hypothetical 10% adverse movement in foreign currency exchange rates would result in a decrease in net income for the three months ended June 30, 2015 of approximately \$0.6 million. There can be no assurances that the above projected exchange rate decrease will materialize. Fluctuations of exchange rates are beyond our control. We will continue to monitor and assess the risk associated with these exposures and may take additional actions in the future to hedge or mitigate these risks.

Credit Risk

Financial instruments that potentially subject us to concentrations of credit risk consist principally of cash equivalents, marketable securities, foreign exchange contracts and accounts receivable. Our cash, cash equivalents and short-term investments are in high-quality securities placed with major banks and financial institutions whom we have evaluated as highly creditworthy, and commercial paper. With respect to accounts receivable, we perform ongoing evaluations of our customers, generally granting uncollateralized credit terms to our customers, and maintaining an allowance for doubtful accounts based on historical experience and our expectation of future losses.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

Our management, including our Chief Executive Officer and Chief Financial Officer, performed an evaluation of our disclosure controls and procedures as required by Rule 13a-15(e) and 15d-15(e) under the Exchange Act. Based on the evaluation as of June 30, 2015, management has concluded that our disclosure controls and procedures were not effective as a result of a material weakness in our internal control over financial reporting as described in Item 9A of our Annual Report on Form 10-K for the year ended December 31, 2014 (the “material weakness”).

We have made progress remediating the material weaknesses which is described below. Notwithstanding the material weaknesses, we believe our consolidated statements presented in this Form 10-Q fairly represent, in all material respects, our financial position, results of operations and cash flows for all periods presented herein.

(b) Changes in Internal Control over Financial Reporting

Except as set forth below, during the six months ended June 30, 2015, there have not been any changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

(c) Plan for Remediation of Material Weakness in Internal Control over Financial Reporting

As previously discussed in our Annual Report on Form 10-K for the year ended December 31, 2014, we are in the process of remediating the material weakness in our internal control over financial reporting. Our remediation plan includes our taking steps to redesign processes and controls to ensure a more precise independent review is performed for manual journal entries and reconciliations, where appropriate, relating to critical calculations and estimates. In addition, we are assessing tools and potential enhancements to document, support and review manual journal entries and account reconciliation processes. We are also evaluating our financial team organizational structure, and what changes to roles and responsibilities we can make to enhance controls and compliance.

Management, with the oversight of the Audit Committee of the Board of Directors, has made substantial progress toward remediation of the material weakness through the following actions:

redesign and implementation of enhanced policies and procedures for preparation and review of account reconciliations;

development of policies and standard procedures for the documentation and review of manual journal entries; and

hiring of temporary resources to provide capacity to fully implement and sustain adherence to redesigned policies and procedures while recruitment of permanent resources are underway.

When fully implemented and operating effectively, we expect these enhancements will remediate the material weakness described above. We have incurred and expect to incur additional costs associated with our remediation efforts. We plan to remediate the material weakness during Fiscal 2015. However, we cannot determine how long it will take to fully and effectively execute our remediation plan, and we cannot provide any assurance that these remediation efforts will be successful or that our internal control over financial reporting will be effective as a result of these efforts.

PART II.**OTHER INFORMATION****Item 1. Legal Proceedings**

We are involved in various investigations, claims and lawsuits arising in the normal conduct of our business, none of which, individually or in the aggregate, in our opinion, will materially harm our business. We cannot assure that we will prevail in any litigation. Regardless of the outcome, any litigation may require us to incur significant litigation expense and may result in significant diversion of our attention.

Item 1A. Risk Factors

In addition to the other information set forth in this Quarterly Report, you should also carefully consider the risk factors discussed in Part I, “Item 1A. Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2014, all of which could materially affect our business, financial condition or operating results and should be considered before making an investment decision regarding our securities. There have been no material changes to these risk factors. The risks described in our Annual Report on Form 10-K are not the only risks facing the Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may adversely affect our business, financial condition or operating results.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchase of Equity Securities

| Period | Total Number of Shares Purchased | Average Price Paid Per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Maximum Number of Shares (or Approximate Dollar Value) that May Yet Be Purchased Under the |
|---------------|---|-------------------------------------|---|---|
|---------------|---|-------------------------------------|---|---|

| | | | | Plans or Programs |
|--------------------------------|--------|----------|--------|--------------------------|
| April 1, 2015 – April 30, 2015 | — | — | — | — |
| May 1, 2015 – May 31, 2015 | 25,413 | \$ 19.26 | 25,413 | \$15.5 million |
| June 1, 2015 – June 30, 2015 | — | — | — | — |
| Total | 25,413 | \$ 19.26 | 25,413 | \$15.5 million |

On February 11, 2015, the Company announced that its Board of Directors had approved a stock buyback program to repurchase up to \$20 million of its common stock in the open market. Purchases are 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.

Item 4. Mine Safety Disclosures

Not applicable.

Item 6. Exhibits

(a) Exhibits.

| Exhibit No. | Description |
|--------------------|---|
| 3.1.1 | Fourth Amended and Restated Articles of Incorporation of Tucows Inc. (Incorporated by reference to Exhibit 3.1 filed with Tucows' Current Report on Form 8-K, as filed with the SEC on November 29, 2007). |
| 3.1.2 | Articles of Amendment to Fourth Amended and Restated Articles of Incorporation of Tucows Inc. (Incorporated by reference to Exhibit 3.1 filed with Tucows' Current Report on Form 8-K, as filed with the SEC on January 3, 2014). |
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| 31.2 | Chief Financial Officer's Rule 13a-14(a)/15d-14(a) Certification * |
| 32.1 | Chief Executive Officer's Section 1350 Certification † |
| 32.2 | Chief Financial Officer's Section 1350 Certification † |
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| 101.SCH | XBRL Taxonomy Extension Schema * |
| 101.CAL | XBRL Taxonomy Extension Calculation * |
| 101.DEF | XBRL Taxonomy Extension Definition * |
| 101.LAB | XBRL Taxonomy Extension Labels * |
| 101.PRE | XBRL Taxonomy Extension Presentation * |

* Filed herewith.

† Furnished herewith.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: August 10, 2015 TUCOWS INC.

By: /s/ Elliot Noss
Elliot Noss
President and Chief Executive Officer

By: /s/ Michael Cooperman
Michael Cooperman Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT INDEX

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