HICKORY TECH CORP
Form 10-Q
May 05, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

ý	**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
	FOR THE QUARTERLY PERIOD ENDED March 31, 2004
	OR
o	**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 0-13721

HICKORY TECH CORPORATION

(Exact name of registrant as specified in its charter)

Minnesota	**41-1524393**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

221 East Hickory Street
Mankato, Minnesota 56002-3248
(Address of principal executive offices and zip code)

(800) 326-5789
(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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 ý No o

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes ý No o

The total number of shares of the registrant s common stock outstanding as of March 31, 2004: 12,975,253.

HICKORY TECH CORPORATION

March 31, 2004

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)

	For Three Months Ended			
(In Thousands Except Per Share Amounts)		**3/31/2004**		**3/31/2003**
OPERATING REVENUES:				
Telecom Sector	$	19,426	$	18,568
Information Solutions Sector		966		1,098
Enterprise Solutions Sector		2,295		3,911
TOTAL OPERATING REVENUES		22,687		23,577
COSTS AND EXPENSES:				
Cost of Products Sold, Enterprise Solutions		1,509		2,519
Cost of Services, excluding Depreciation and Amortization		8,608		8,268
Selling, General and Administrative Expenses, excluding Depreciation and Amortization		3,656		3,824
Depreciation		3,876		3,502
Amortization of Intangibles		236		326
TOTAL COSTS AND EXPENSES		17,885		18,439
OPERATING INCOME		4,802		5,138
OTHER INCOME/(EXPENSE):				
Equity in Net Loss of Investees				(3)
Interest and Other Income		15		9
Interest Expense		(1,189)		(1,565)
TOTAL OTHER INCOME/(EXPENSE)		(1,174)		(1,559)
INCOME BEFORE INCOME TAXES		3,628		3,579
INCOME TAX PROVISION		1,467		1,462
INCOME FROM CONTINUING OPERATIONS		2,161		2,117
DISCONTINUED OPERATIONS (Note 4)				
Income/(Loss) from Operations of Discontinued Component		(99)		390
Income Tax (Benefit)/Provision		(40)		160
INCOME/(LOSS) FROM DISCONTINUED OPERATIONS		(59)		230
NET INCOME	$	2,102	$	2,347
Basic Earnings Per Share - Continuing Operations:	$	0.17	$	0.15
Basic Earnings/(Loss) Per Share - Discontinued Operations:		(0.01)		0.02
	$	0.16	$	0.17
Dividends Per Share	$	0.11	$	0.11

Weighted Average Common Shares Outstanding		12,970		13,994
Diluted Earnings Per Share - Continuing Operations:	$	0.17	$	0.15
Diluted Earnings/(Loss) Per Share - Discontinued Operations:		(0.01)		0.02
	$	0.16	$	0.17
Weighted Average Common and Equivalent Shares Outstanding		13,020		14,007

The accompanying notes are an integral part of the consolidated financial statements.

HICKORY TECH CORPORATION

March 31, 2004

CONSOLIDATED BALANCE SHEETS

(UNAUDITED)

(In Thousands Except Share and Per Share Amounts)		**3/31/2004**		**12/31/2003**
ASSETS				
CURRENT ASSETS:				
Cash and Cash Equivalents	**$**	**143**	$	278
Receivables, Net of Allowance for Doubtful Accounts of $1,265 and $1,283		**9,803**		9,984
Income Taxes Receivable				2,838
Costs in Excess of Billings on Contracts		**333**		934
Inventories		**4,400**		4,453
Deferred Income Taxes		**1,057**		1,057
Other		**2,033**		2,497
TOTAL CURRENT ASSETS		**17,769**		22,041
INVESTMENTS		**4,371**		6,710
PROPERTY, PLANT AND EQUIPMENT		**232,447**		230,490
Less ACCUMULATED DEPRECIATION		**120,211**		116,487
PROPERTY, PLANT AND EQUIPMENT, NET		**112,236**		114,003
OTHER ASSETS:				
Goodwill		**25,086**		25,086
Intangible Assets, Net		**456**		481
Financial Derivative Instruments		**1,038**		2,515
Deferred Costs and Other		**4,532**		4,876
TOTAL OTHER ASSETS		**31,112**		32,958
TOTAL ASSETS	**$**	**165,488**	$	175,712
LIABILITIES & SHAREHOLDERS EQUITY				
CURRENT LIABILITIES:				
Cash Overdraft	**$**	**28**	$	1,001
Accounts Payable		**2,868**		3,771
Accrued Expenses		**3,361**		3,243
Accrued Interest		**62**		41
Accrued Income Taxes		**334**		
Billings in Excess of Costs on Contracts		**200**		73
Advanced Billings and Deposits		**3,076**		3,040
Current Maturities of Long-Term Obligations		**1,506**		1,572
TOTAL CURRENT LIABILITIES		**11,435**		12,741
LONG-TERM OBLIGATIONS, Net of Current Maturities		**109,643**		118,040
DEFERRED INCOME TAXES		**9,720**		10,331
DEFERRED REVENUE AND EMPLOYEE BENEFITS		**6,011**		5,883
TOTAL LIABILITIES		**136,809**		146,995

COMMITMENTS AND CONTINGENCIES (Note 9)				
SHAREHOLDERS EQUITY:				
Common Stock, no par value, $.10 stated value Shares authorized: 100,000,000 Shares outstanding: 12,975,253 in 2004 and 12,967,811 in 2003		**1,298**		1,297
Additional Paid-In Capital		**7,842**		7,690
Retained Earnings		**18,921**		18,246
Accumulated Other Comprehensive Income		**618**		1,484
TOTAL SHAREHOLDERS EQUITY		**28,679**		28,717
TOTAL LIABILITIES & SHAREHOLDERS EQUITY	**$**	**165,488**	$	175,712

The accompanying notes are an integral part of the consolidated financial statements.

HICKORY TECH CORPORATION

March 31, 2004

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)

	For Three Months Ended	
(Dollars In Thousands)	**3/31/2004**	**3/31/2003**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	**$ 2,102**	$ 2,347
Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities:		
Depreciation and Amortization	**4,112**	4,488
Gain on Sale of Assets		(1)
Stock-Based Compensation	**35**	257
Employee Retirement Benefits and Deferred Compensation	**166**	(34)
Accrued Patronage Refunds	**(107)**	(181)
Equity in Net Loss of Investees		3
Provision for Losses on Accounts Receivable	**144**	235
Changes in Operating Assets and Liabilities:		
Receivables	**3,208**	2,995
Inventories	**53**	131
Billings and Costs on Contracts	**729**	479
Accounts Payable and Accrued Expenses	**(764)**	(1,787)
Advance Billings and Deposits	**36**	(3)
Deferred Revenue and Employee Benefits	**(38)**	(29)
Other	**443**	377
Net Cash Provided By Operating Activities	**10,119**	9,277
CASH FLOWS FROM INVESTING ACTIVITIES:		
Additions to Property, Plant and Equipment	**(2,122)**	(1,735)
Redemption of Investments	**2,600**	4,100
Proceeds from Sale of Assets	**12**	60
Net Cash Provided By Investing Activities	**490**	2,425
CASH FLOWS FROM FINANCING ACTIVITIES:		
Change in Cash Overdraft	**(973)**	
Payments of Capital Lease Obligations	**(213)**	(145)
Repayments on Credit Facility	**(9,250)**	(9,750)
Borrowings on Credit Facility	**1,000**	
Proceeds from Issuance of Common Stock	**118**	131
Dividends Paid	**(1,426)**	(1,540)
Stock Repurchase		(161)
Net Cash Used In Financing Activities	**(10,744)**	(11,465)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**(135)**	237

CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD		**278**		1,874
CASH AND CASH EQUIVALENTS AT END OF PERIOD	**$**	**143**	$	2,111
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:				
Cash Paid for Interest	**$**	**1,236**	$	1,734
Cash Paid for Income Taxes, Net of Tax Refunds of $1,750 and $1,600 in 2004 and 2003	**$**	**(1,745)**	$	(1,600)

The accompanying notes are an integral part of the consolidated financial statements.

HICKORY TECH CORPORATION

MARCH 31, 2004

PART 1. FINANCIAL INFORMATION

ITEM 1. NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. BASIS OF PRESENTATION

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information necessary for a fair presentation of results of operations, financial position, and cash flows in conformity with accounting principles generally accepted in the United States of America. In the opinion of management, the condensed consolidated financial statements reflect all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation of Hickory Tech Corporation s (HickoryTech) results for the periods presented. Operating results for interim periods are not necessarily indicative of results that may be expected for the fiscal year as a whole. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and related disclosures at the date of the financial statements and during the reporting period. Actual results could differ from these estimates. These unaudited interim condensed consolidated financial statements should be read in conjunction with HickoryTech s Annual Report on Form 10-K for the year ended December 31, 2003.

The condensed consolidated financial statements of HickoryTech include Hickory Tech Corporation and its subsidiaries in the following three business segments: (i) Telecom Sector, (ii) Information Solutions Sector and (iii) Enterprise Solutions Sector. During the first quarter of 2003, the Information Solutions Sector had an investment in an unconsolidated partnership, which was accounted for using the equity method. This partnership was dissolved in the fourth quarter of 2003. All inter-company transactions have been eliminated from the consolidated financial statements.

Certain expenses reported as operating expenses in 2003 have been reclassified between cost of services and selling, general and administrative expenses to conform to the 2004 presentation. These reclassifications did not change previously reported net income, shareholders equity or cash flows.

Cost of services include all costs related to delivery of HickoryTech s communications services and products. These costs include all costs of performing services and providing related products. It does not include costs associated with selling, general and administrative, depreciation and amortization of property, plant and equipment and intangible assets, and cost of products sold for the Enterprise Solutions Sector.

On December 15, 2003, HickoryTech sold its wireless business, Minnesota Southern Wireless Company (MSWC), to Western Wireless Corporation (WWC). The wireless operations are reported as part of the Telecom Sector. The results of operations of the wireless business are reported as discontinued operations for all periods presented (see Note 4).

NOTE 2. EARNINGS AND CASH DIVIDENDS PER COMMON SHARE

Basic earnings per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during the applicable period. Shares used in the earnings per share assuming dilution calculation are based on the weighted average number of shares of common stock outstanding during the quarter increased by potentially dilutive common shares. Potentially dilutive common shares include stock options and stock subscribed under the employee stock purchase plan (ESPP).

	For Three Months Ended	
	3/31/2004	**3/31/2003**
Weighted Average Shares Outstanding	12,969,590	13,993,696
Stock Options (dilutive only)	37,350	2,535
Stock Subscribed (ESPP)	12,958	11,095
Total Dilutive Shares Outstanding	13,019,898	14,007,326

Options to purchase 406,433 and 555,835 shares for the three months ended March 31, 2004 and 2003, respectively, were not included in the computation of earnings per share assuming dilution because their effect on earnings per share would have been antidilutive.

Cash dividends are based on the number of common shares outstanding at the respective record dates. Listed below is the number of shares outstanding as of the record date for the first quarter of 2004 and 2003.

Shares Outstanding on Record Date	**2004**	**2003**
First Quarter (Feb. 15)	12,967,886	14,003,335

Dividends per share are based on the quarterly dividend per share as declared by the HickoryTech Board of Directors.

During the first three months of 2004 and 2003, shareholders have elected to reinvest $67,000 and $66,000, respectively, of dividends into HickoryTech common stock pursuant to the HickoryTech Dividend Reinvestment Plan.

NOTE 3. COMPREHENSIVE INCOME

HickoryTech follows the provisions of SFAS No. 130, Reporting Comprehensive Income. This statement established rules for the reporting of comprehensive income and its components. In addition to net income, HickoryTech s comprehensive income includes changes in unrealized gains and losses on derivative instruments qualifying and designated as cash flow hedges. Comprehensive income for the three months ended March 31, 2004 and 2003 was $1,236,000 and $2,347,000, respectively.

NOTE 4. DISCONTINUED OPERATIONS

On December 15, 2003, HickoryTech sold its wireless business, Minnesota Southern Wireless Company (MSWC), to Western Wireless Corporation (WWC). The wireless operations are reported as part of the Telecom Sector. The consolidated statements of operations for all periods presented have been restated to reflect wireless operations as discontinued operations.

Wireless business revenue and income before income taxes included in discontinued operations are as follows:

	For Three Months Ended	
(Dollars in Thousands)	**3/31/2004**	**3/31/2003**
Revenues	$	$ 3,393
Income/(Loss) Before Income Taxes	$ (99)	$ 390

NOTE 5. INVENTORIES

Inventories, which consist of equipment for resale, materials and supplies, are stated at the lower of average cost or market. Cost is determined on a first-in first-out (FIFO) basis. The net realizable value of the inventory is reflected by reserves, which offset the cost of inventory.

NOTE 6. INTANGIBLE ASSETS

Effective January 1, 2002, HickoryTech adopted SFAS No. 142, Goodwill and Other Intangible Assets. SFAS No. 142 established new standards related to how acquired goodwill and other intangible assets are to be recorded upon their acquisition as well as how they are to be accounted for after they have been initially recognized in the financial statements.

Effective with the adoption of this standard, HickoryTech is no longer amortizing acquired goodwill. Instead, SFAS No. 142 requires acquired goodwill to be evaluated for impairment using a two-step test based upon a fair value approach. The first step is used to identify potential impairment based upon the fair value of the applicable reporting unit. If the fair value of the reporting unit is less than its carrying value, a second step is required to determine the fair value of the individual assets and liabilities of the reporting unit in order to measure the amount of the goodwill impairment. Upon adoption of this standard, HickoryTech completed a transitional impairment test for its acquired goodwill, determining fair value using primarily a discounted cash flow model. The determined fair value was sufficient to pass the first step impairment test, and therefore no impairment was recorded.

On a prospective basis, HickoryTech is required to test acquired goodwill for impairment on an annual basis based upon a fair value approach. Additionally, goodwill shall be tested for impairment between annual tests if an event occurs or circumstances change that would more likely than not reduce the fair value of an entity below its carrying value. Other indefinite-lived intangible assets will be tested between annual tests if events or changes in circumstances indicate that the asset might be impaired.

The carrying value of HickoryTech s goodwill is $25,086,000 as of March 31, 2004 and December 31, 2003.

The components of HickoryTech s other intangible assets are shown in the following table:

	As of March 31, 2004		As of December 31, 2003	
(Dollars in Thousands)	**Gross Carrying Amount**	**Accumulated Amortization**	**Gross Carrying Amount**	**Accumulated Amortization**
Definite-Lived Intangible Assets				
Customers	$ 821	$ 365	$ 821	$ 340
Other Intangibles	100	100	100	100
Total	$ 921	$ 465	$ 921	$ 440

Amortization expense related to the definite-lived intangible assets for the three months ended March 31, 2004 and 2003 was $25,000 and $26,000, respectively. Total estimated amortization expense for the remaining nine months of 2004 and the five years subsequent to 2004 is as follows: 2004 (April 1 through December 31) - $77,000; 2005 - $102,000; 2006 - $102,000; 2007 - $102,000; 2008 - $73,000 and 2009 - $0.

NOTE 7. RECENT ACCOUNTING DEVELOPMENTS

In January 2003, the FASB issued FIN No. 46, *Consolidation of Variable Interest Entities*. This interpretation provides guidance on how to identify a variable interest entity and addresses when the assets, liabilities and results of operations of such entities must be included in a company s consolidated financial statements. This interpretation was effective immediately for variable interest entities created after January 31, 2003 and for variable interest entities in which the Company obtains an interest after that date. For interests in variable interest entities that were acquired prior to January 31, 2003, the Company adopted the provisions of this interpretation on July 1, 2003. Adoption of this statement did not result in the consolidation or disclosure of any variable interest entities in which the Company maintains an interest. The Company did not absorb the majority of the losses or residual returns of the variable interest entities in which the Company maintains an interest and these interests are not significant. In December 2003, the FASB issued a revised FIN No. 46 which clarifies certain aspects of the accounting for variable interest entities. The revision of FIN No. 46 had no impact on our results of operations or financial position.

In January 2004, the FASB issued FASB Staff Position (FSP) No. FAS 106-1, *Accounting and Disclosure Requirements Related to the Medicare Prescription Drug Improvement and Modernization Act of 2003*. This FSP outlines the appropriate accounting treatment for the effects of the new Medicare law, as well as the required financial statement disclosures. The new law introduces a prescription drug benefit under Medicare, as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to the Medicare plan. The retiree medical plans do provide prescription drug coverage. However, as permitted by FSP No. FAS 106-1, the Company has elected to defer recognition of the impacts of the new law on the accumulated post-retirement benefit obligation and net periodic post-retirement benefit expense presented in the consolidated financial statements. Specific authoritative accounting guidance on the accounting for the federal subsidy provided for in the Act is pending. That guidance, when issued, could require the Company to change previously reported information. Beginning January 1, 2006, Medicare s prescription drug plan will be the primary plan for qualified retirees when they become age 65 and are eligible for Medicare. Thus, the Company may see a decrease in the amount of prescription drug benefits to be paid beginning in 2006.

In December 2003, the FASB issued a revision of SFAS No. 132, *Employers Disclosures about Pensions and Other Post-retirement Benefits*. This statement revises the disclosures required for pension and other post-retirement benefit plans. The Company has incorporated the new disclosure requirements into the Notes to Consolidated Financial Statements included in this report.

NOTE 8. QUARTERLY SECTOR FINANCIAL SUMMARY

(Dollars In Thousands)	Telecom	Information Solutions	Enterprise Solutions	Corporate and Eliminations	HickoryTech Consolidated
Three Months Ended 3/31/04					
Operating Revenue from Unaffiliated Customers	$ 19,426	$ 966	$ 2,295	$	$ 22,687
Intersegment Revenues	69	1,047		(1,116)	
Total	19,495	2,013	2,295	(1,116)	22,687
Depreciation and Amortization	3,407	639	51	15	4,112
Operating Income (Loss)	6,079	(706)	(376)	(195)	4,802
Interest Expense	3	13		1,173	1,189
Income Taxes (Benefit)	2,460	(290)	(152)	(551)	1,467
Income (Loss) from Continuing Operations	3,619	(426)	(224)	(808)	2,161
Loss from Discontinued Operations Including Intersegment Revenues	(59)				(59)
Net Income (Loss)	3,560	(426)	(224)	(808)	2,102
Identifiable Assets	143,933	7,483	7,714	6,358	165,488
Property, Plant and Equip., Net	106,782	4,865	409	180	112,236
Capital Expenditures	2,121	1			2,122
Three Months Ended 3/31/03					
Operating Revenue from Unaffiliated Customers	$ 18,568	$ 1,098	$ 3,911	$	$ 23,577
Intersegment Revenues	69	763		(832)	
Total	18,637	1,861	3,911	(832)	23,577
Depreciation and Amortization	3,185	544	61	38	3,828
Operating Income (Loss)	6,304	(749)	74	(491)	5,138
Interest Expense	5	18		1,542	1,565
Income Taxes (Benefit)	2,660	(259)	27	(966)	1,462
Income (Loss) from Continuing Operations	3,708	(496)	39	(1,134)	2,117
Income from Discontinued Operations Including Intersegment Revenues	65	124		41	230
Net Income (Loss)	3,773	(372)	39	(1,093)	2,347
Identifiable Assets	148,793	8,917	9,363	9,197	176,270
Property, Plant and Equip., Net	110,307	5,845	537	212	116,901
Capital Expenditures	1,051	144	92	127	1,414

The Telecom Segment Identifiable Assets, Property Plant and Equipment and Capital Expenditures presented above, exclude the following amounts related to the wireless business, which is reported as a discontinued operation:

	Three Months Ended	
(Dollars in Thousands)	**3/31/2004**	**3/31/2003**
Identifiable Assets	$	$ 53,286
Property, Plant and Equip., Net	$	$ 16,888
Capital Expenditures	$	$ 321

NOTE 9. CONTINGENCIES

HickoryTech is involved in certain contractual