

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

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

For the quarterly period ended March 31, 2018

**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: 001-32421**

**FUSION CONNECT, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation or organization)

**58-2342021**

(IRS Employer Identification No.)

**420 Lexington Avenue, Suite 1718, New York, New York 10170**

(Address of principal executive offices) (Zip Code)

**(212) 201-2400**

(Registrants telephone number, including area code)

**Fusion Telecommunications International, Inc.**

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

Indicate by check mark whether the issuer (1) has filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act 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, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer", "accelerated filer", "non-accelerated filer", "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input checked="" type="checkbox"/>
(do not check if a smaller reporting company)		Emerging growth company	<input type="checkbox"/>

If an emerging growth company that prepares its financial statements in accordance with U.S. GAAP, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: May 7, 2018.

<b>Title of Each Class</b>	<b>Number of Shares Outstanding</b>
Common Stock, \$0.01 par value	76,583,701

FUSION CONNECT, INC. AND SUBSIDIARIES

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FUSION CONNECT, INC. AND SUBSIDIARIES

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

Condensed Consolidated Balance  
Sheets

	March 31, 2018	December 31, 2017
	(unaudited)	
<b>ASSETS</b>		
<b>Current assets:</b>		
Cash and cash equivalents	\$ 30,999,732	\$ 2,472,836
Accounts receivable, net of allowance for doubtful accounts of approximately \$435,000 and \$668,000, respectively	9,174,993	10,634,393
Prepaid expenses and other current assets	1,871,183	1,609,518
Deferred installation costs - current portion	798,166	-
Current assets of discontinued operations	4,269,653	2,867,953
<b>Total current assets</b>	<b>47,113,727</b>	<b>17,584,700</b>
Property and equipment, net	11,115,107	12,838,840
Security deposits	612,299	612,299
Restricted cash	27,153	27,153
Goodwill	35,181,698	34,773,629
Intangible assets, net	55,687,545	56,156,023
Deferred installation costs - net of current portion	1,102,648	-
Other assets	35,632	43,937
Non-current assets of discontinued operations	19,780	20,980
<b>TOTAL ASSETS</b>	<b><u>\$150,895,589</u></b>	<b><u>\$122,057,561</u></b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)</b>		
<b>Current liabilities:</b>		
Term loan - current portion	\$ 6,500,000	\$ 6,500,000
Obligations under asset purchase agreements - current portion	723,297	227,760
Equipment financing obligations - current portion	1,075,252	1,206,773
Deferred installation revenue - current portion	797,332	-
Accounts payable and accrued expenses	20,165,445	21,995,443
Current liabilities from discontinued operations	4,660,278	3,093,602
<b>Total current liabilities</b>	<b><u>33,921,604</u></b>	<b><u>33,023,578</u></b>
<b>Long-term liabilities:</b>		
Notes payable - non-related parties, net of discount	32,083,554	31,953,163
Notes payable - related parties	928,081	928,081
Term loan	47,663,242	54,222,668
Indebtedness under revolving credit facility	-	1,500,000
Obligations under asset purchase agreements	477,162	222,240
Equipment financing obligations - net of current obligations	407,345	590,602
Deferred installation revenue - net of current portion	1,029,445	-
Derivative liabilities	586,197	872,900
<b>Total liabilities</b>	<b><u>117,096,630</u></b>	<b><u>123,313,232</u></b>
<b>Stockholders' equity (deficit):</b>		
Preferred stock, \$0.01 par value, 10,000,000 shares authorized, 13,466 and 14,216 shares issued and outstanding	134	142
Common stock, \$0.01 par value, 150,000,000 shares authorized, 23,847,140 and 14,980,756 shares issued and outstanding	238,471	149,807
Capital in excess of par value	235,027,397	195,940,320
Accumulated deficit	(201,318,706)	(197,264,083)
Total Fusion Connect, Inc. stockholders' equity (deficit)	33,947,296	(1,173,804)
Noncontrolling interest	(148,337)	(81,867)
<b>Total stockholders' equity (deficit)</b>	<b><u>33,798,959</u></b>	<b><u>(1,255,671)</u></b>
<b>TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT)</b>	<b><u>\$150,895,589</u></b>	<b><u>\$122,057,561</u></b>

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

FUSION CONNECT, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Operations  
(unaudited)

	For the Three Months Ended March 31,	
	2018	2017
<b>Revenues</b>	\$ 29,038,043	\$ 28,481,039
Cost of revenues, exclusive of depreciation and amortization, shown separately below	12,918,895	12,140,707
<b>Gross profit</b>	16,119,148	16,340,332
Depreciation and amortization	3,135,779	3,835,948
Selling, general and administrative expenses	13,947,995	13,613,661
Impairment charge	1,195,837	-
Total operating expenses	18,279,611	17,449,609
<b>Operating loss</b>	<u>(2,160,463)</u>	<u>(1,109,277)</u>
<b>Other (expenses) income:</b>		
Interest expense	(2,147,775)	(2,092,312)
Change in fair value of derivative liabilities	194,312	(40,445)
Loss on disposal of property and equipment	(3,184)	(26,800)
Other income, net	89,558	116,520
Total other expenses	<u>(1,867,089)</u>	<u>(2,043,037)</u>
Loss before income taxes	(4,027,552)	(3,152,314)
Provision for income taxes	(14,050)	(7,811)
<b>Net loss from continuing operations</b>	(4,041,602)	(3,160,125)
<b>Net loss from discontinued operations</b>	<u>(166,175)</u>	<u>(321,823)</u>
<b>Net loss</b>	(4,207,777)	(3,481,948)
Less: Net loss attributable to non-controlling interest	66,470	-
<b>Net loss attributable to Fusion Connect, Inc.</b>	(4,141,307)	(3,481,948)
Preferred stock dividends	(243,582)	(1,254,109)
<b>Net loss attributable to common stockholders</b>	<u>(4,384,889)</u>	<u>(4,736,057)</u>
<b>Basic and diluted loss per common share from continuing operations:</b>	\$ (0.20)	\$ (0.32)
<b>Basic and diluted loss per common share from discontinued operations:</b>	\$ (0.01)	\$ (0.02)
<b>Weighted average common shares outstanding:</b>		
Basic and diluted	<u>20,682,262</u>	<u>13,805,133</u>

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

**FUSION CONNECT, INC. AND SUBSIDIARIES**

**Condensed Consolidated Statement of Stockholders' (Deficit) Equity  
(unaudited)**

	Preferred Stock		Common Stock		Capital in	Accumulated	Total Fusion	Non-	Stockholders'
	Shares	\$	Shares	\$	Excess of Par	Deficit	Connect, Inc. (Deficit)	controlling	(Deficit)
					Value		Equity	interest	Equity
Balance at December 31, 2017	14,216	\$ 142	14,980,756	149,807	\$ 195,940,330	\$(197,264,083)	\$ (1,173,804)	\$ (81,867)	\$ (1,255,671)
Cumulative effect of change in accounting principle	-	-	-	-	-	86,684	86,684	-	86,684
Balance at January 1, 2018	14,216	142	14,980,756	149,807	195,940,330	(197,177,399)	(1,087,120)	(81,867)	(1,168,987)
Conversion of preferred stock into common stock	(750)	(8)	100,000	1,000	(992)	-	-	-	-
Dividends on preferred stock	-	-	3,985	40	(40)	-	-	-	-
Exercise of common stock purchase warrants	-	-	5,120	51	11,931	-	11,982	-	11,982
Cashless exercise of warrants	-	-	22,155	222	(222)	-	-	-	-
Reclassification of derivative liability	-	-	-	-	92,391	-	92,391	-	92,391
Common stock issued in acquisition	-	-	110,124	1,101	498,899	-	500,000	-	500,000
Proceeds from the sale of common stock, less expenses of \$2,843,000	-	-	8,625,000	86,250	38,119,846	-	38,206,096	-	38,206,096
Net loss	-	-	-	-	-	(4,141,307)	(4,141,307)	(66,470)	(4,207,777)
Stock-based compensation	-	-	-	-	365,254	-	365,254	-	365,254
Balance at March 31, 2018	<u>13,466</u>	<u>\$ 134</u>	<u>23,847,140</u>	<u>\$ 238,471</u>	<u>\$ 235,027,397</u>	<u>\$(201,318,706)</u>	<u>\$ 33,947,296</u>	<u>\$ (148,337)</u>	<u>\$ 33,798,959</u>

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

FUSION CONNECT, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows  
(unaudited)

	<b>Three Months Ended March 31,</b>	
	<b>2018</b>	<b>2017</b>
<b>Cash flows from operating activities:</b>		
Net loss from continuing operations	\$ (4,041,602)	\$ (3,160,125)
Net loss from discontinued operations	(166,175)	(321,823)
Net loss	<u>(4,207,777)</u>	<u>(3,481,948)</u>
<b>Adjustments to reconcile net loss to net cash provided by (used in) operating activities:</b>		
Depreciation and amortization	3,135,779	3,835,948
Loss on disposal of property and equipment	3,184	26,800
Stock-based compensation	365,254	224,647
Impairment charge	1,195,837	-
Stock issued for services rendered or in settlement of liabilities	-	164,450
Amortization of debt discount and deferred financing fees	195,963	209,628
(Gain) loss on the change in fair value of derivative liability	(194,312)	40,445
<b>Changes in operating assets and liabilities:</b>		
Accounts receivable	1,459,401	179,518
Prepaid expenses and other current assets	(304,442)	(873,401)
Other assets and liabilities	20,952	8,295
Accounts payable and accrued expenses	<u>(1,949,917)</u>	<u>690,812</u>
Cash (used in) provided by operating activities - continuing operations	(113,903)	1,385,070
Cash provided by (used in) operating activities - discontinued operations	<u>107,612</u>	<u>(15,826)</u>
<b>Net cash (used in) provided by operating activities</b>	<u>(6,291)</u>	<u>1,369,244</u>
<b>Cash flows from investing activities:</b>		
Purchase of property and equipment	(976,877)	(984,642)
Proceeds from the sale of property and equipment	31,533	40,680
(Payment) for acquisitions, net of cash acquired	-	(558,329)
Cash used in investing activities - continuing operations	<u>(945,344)</u>	<u>(1,502,291)</u>
Cash used in investing activities - discontinued operations	-	-
<b>Net cash used in investing activities</b>	<u>(945,344)</u>	<u>(1,502,291)</u>
<b>Cash flows from financing activities:</b>		
Proceeds from the exercise of common stock purchase warrants	11,982	780,951
Repayments of term loan	(6,625,000)	(812,500)
Repayments of revolving debt, net	(1,500,000)	-
Payments for obligations under asset purchase agreements	(192,157)	(191,668)
Proceeds from the sale of common stock, net of offering expenses	38,206,096	-
Payments on equipment financing obligations	<u>(314,777)</u>	<u>(223,493)</u>
Cash provided by (used in) financing activities - continuing operations	29,586,144	(446,710)
Cash provided by (used in) financing activities - discontinued operations	-	-
<b>Net cash provided by (used in) financing activities</b>	<u>29,586,144</u>	<u>(446,710)</u>
<b>Net change in cash and cash equivalents</b>	<u>28,634,509</u>	<u>(579,757)</u>
<b>Cash and cash equivalents, including restricted cash, beginning of period</b>	<u>2,557,541</u>	<u>7,249,063</u>
<b>Cash and cash equivalents, including restricted cash, end of period</b>	<u>\$ 31,192,050</u>	<u>\$ 6,669,306</u>
<b>Less cash and cash equivalents of discontinued operations, end of period</b>	<u>165,165</u>	<u>15,038</u>
<b>Cash and cash equivalents, including restricted cash of continuing operations, end of period</b>	<u><u>31,026,885</u></u>	<u><u>6,654,268</u></u>

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

**Note 1. Organization and Business**

Fusion Connect, Inc. (f/k/a Fusion Telecommunications International, Inc.) is a Delaware corporation incorporated in September 1997 (“Fusion” and together with its subsidiaries, the “Company,” “we,” “us” and “our”). Fusion changed its name to Fusion Connect, Inc. on May 4, 2018. The Company is a provider of integrated cloud solutions, including cloud voice, cloud connectivity, cloud infrastructure, cloud computing, and managed cloud-based applications to businesses of all sizes.

**Note 2. Basis of Presentation and Summary of Significant Accounting Policies**

**Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements have been prepared in all material respects in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) for interim financial information. Pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (the “SEC”), certain information and footnote disclosures normally included in annual consolidated financial statements prepared in accordance with U.S. GAAP have been condensed or omitted.

Because certain information and footnote disclosures have been condensed or omitted, these unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and related notes contained in the Company’s Annual Report on Form 10-K for the fiscal year ended December 31, 2017 (the “2017 Form 10-K”) as filed with the SEC. In management’s opinion, all normal and recurring adjustments considered necessary for a fair presentation of the financial position, results of operations and cash flows for the periods presented have been included. Management believes that the disclosures made in these unaudited condensed consolidated interim financial statements are adequate to make the information not misleading. The results of operations for the interim periods presented are not necessarily indicative of the results for the entire year.

On May 4, 2018 (the “Closing Date”), Fusion completed the various transactions contemplated by the Agreement and Plan of Merger, dated August 26, 2017, as amended (the “Birch Merger Agreement”), by and among Fusion, Fusion BCHI Acquisition LLC, a wholly-owned subsidiary of Fusion (“BCHI Merger Sub”), and Birch Communications Holdings, Inc. (“Birch”). As contemplated by the Birch Merger Agreement, on the Closing Date, Birch merged with and into BCHI Merger Sub (the “Birch Merger”), with BCHI Merger Sub surviving the Birch Merger as a wholly-owned subsidiary of Fusion. See “Note 19 – Subsequent Events”.

The Company determined that the acquisition of Birch qualified as a reverse acquisition where Fusion was identified as a legal acquirer and Birch was identified as an accounting acquirer. All periodic reports for periods that end on or after the date the reverse acquisition is completed will be filed within the time periods specified by the SEC’s rules and forms. The financial statements included in periodic reports filed for periods that end on or after the date the reverse acquisition is completed will be the accounting acquirer’s financial statements for all periods presented (reflecting the combined company beginning with the date of the reverse acquisition) since the accounting acquirer is considered to be the successor to the legal issuer’s reporting obligation.

In the quarter ended March 31, 2018, the Company determined that the assets and liabilities of its Carrier Services reportable segment met the discontinued operations criteria in ASC 205-20-45. Accordingly, all assets, liabilities and results of operations have been classified as discontinued operations for all periods presented in the accompanying Consolidated Balance Sheet, Consolidated Statements of Operations and Consolidated Statements of Cash Flows. See “Note 3 - Discontinued Operations”.

During the three months ended March 31, 2018 and 2017, comprehensive loss was equal to the net loss amounts presented for the respective periods in the accompanying condensed consolidated interim statements of operations.

***Reverse Stock Split***

Fusion filed a Certificate of Amendment (the “Charter Amendment”) to its Certificate of Incorporation with the Secretary of State of the State of Delaware, to effect a reverse split of the Fusion common stock at an exchange ratio of 1-for-1.5 (the “Reverse Split”), which became effective on May 4, 2018. The number of authorized shares of Fusion common stock was not affected by the Reverse Split. Any fractional shares of Fusion common stock resulting from the Reverse Split were rounded up to the nearest whole share.

As a result of the Reverse Stock Split, all share and per share amounts as of December 31, 2017 as well as for the three months ended March 31, 2018 and March 31, 2017, have been restated at the Reverse Split Ratio to give effect to the Reverse Stock Split.

**Principles of Consolidation**

The condensed consolidated interim financial statements include the accounts of Fusion and each of its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation. Effective September 1, 2017, Fusion transferred 40% of its membership interests in Fusion Global Services LLC (“FGS”) to XcomIP, LLC (“XcomIP”), in exchange for which XcomIP contributed assets of its carrier business to FGS. In connection with this transaction, Fusion and XcomIP also executed a shareholder agreement under which Fusion agreed to provide up to \$750,000 in working capital to FGS. The Company has determined that, based on the terms of the shareholders agreement, it has a controlling financial interest in FGS under the guidance set forth in Accounting Standards Codification (“ASC”) 810, Consolidation and, therefore, the accounts of FGS are consolidated into Fusion’s consolidated financial statements as of and for the year ended December 31, 2017. Prior to the transfer of membership interests to XcomIP, Fusion transferred its Carrier Services business to FGS. Effective March 31, 2018, the Carrier Business is recorded as discontinued operations for all periods presented. See “Note 19 – Subsequent Events”.

**Use of Estimates**

The preparation of condensed consolidated interim financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated interim financial statements and the reported amounts of revenues and expenses during the reporting periods. On an on-going basis, the Company evaluates its estimates, including, but not limited to, those related to recognition of revenue; allowance for doubtful accounts; fair value measurements of its financial instruments; useful lives of its long-lived assets used in computing depreciation and amortization; impairment assessment of goodwill and intangible assets; accounting for stock options and other equity awards, particularly related to fair value estimates; and accounting for income taxes, contingencies and litigation. Changes in the facts or circumstances underlying these estimates could result in material changes and actual results could differ from those estimates.

**Cash Equivalents**

Cash and cash equivalents include cash on deposit and short-term, highly-liquid investments with maturities of three months or less on the date of purchase. As of March 31, 2018 and December 31, 2017, the carrying value of cash and cash equivalents approximates fair value due to the short period to maturity.

**Fair Value of Financial Instruments**

At March 31, 2018 and December 31, 2017, the carrying value of the Company’s accounts receivable, accounts payable and accrued expenses approximates their fair value due to the short-term nature of these financial instruments.

**Impairment of Long-Lived Assets**

The Company periodically reviews long-lived assets, including intangible assets, for possible impairment when events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If an impairment indicator is present, the Company evaluates recoverability by a comparison of the carrying amount of the assets to future undiscounted net cash flows expected to be generated by the assets. If the carrying value of the asset exceeds the projected undiscounted cash flows, the Company is required to estimate the fair value of the asset and recognize an impairment charge to the extent that the carrying value of the asset exceeds its estimated fair value. During the three-month period ended March 31, 2018, the Company recorded an impairment charge of \$1.2 million. The Company did not record any impairment charges during the three months ended March 31, 2017.

**Goodwill**

Goodwill is the excess of the acquisition cost of a business combination over the fair value of the identifiable net assets acquired. Goodwill at March 31, 2018 and December 31, 2017 was \$35.2 million and \$34.8 million, respectively. All of the Company’s goodwill is attributable to its Business Services segment.

The following table presents the changes in the carrying amounts of goodwill during the three months ended March 31, 2018:

Balance at December 31, 2017	\$ 34,773,629
Increase in goodwill associated with a business acquisition	408,069
Balance at March 31, 2018	<u>\$ 35,181,698</u>

Goodwill is not amortized and is tested for impairment on an annual basis in the fourth quarter of each fiscal year and whenever events or circumstances indicate that it is more likely than not that fair value of a reporting unit is below its carrying amount.

The Company has the option to perform a qualitative assessment of goodwill to determine whether it is more likely than not that the fair value of its reporting unit is less than its carrying amount, including goodwill and other intangible assets. The Company also may elect not to perform the qualitative assessment and, instead, proceed directly to the quantitative impairment test by comparing the fair value of the reporting unit to its carrying value. An impairment charge is recorded to the extent the reporting unit's carrying value exceeds its fair value, however, the impairment loss recognized would not exceed the total amount of goodwill allocated to that reporting unit. The Company did not record any impairment charges related to goodwill during the three months ended March 31, 2018 and 2017.

#### **Advertising and Marketing Costs**

Advertising and marketing expenses includes cost for promotional materials and trade show expenses for the marketing of the Company's products and services. Advertising and marketing expenses were \$0.1 million for each of the three months ended March 31, 2018 and 2017. Advertising and marketing expenses are reflected in selling, general and administrative expenses in the Company's condensed consolidated statements of operations.

#### **Income Taxes**

The accounting and reporting requirements with respect to accounting for income taxes require an asset and liability approach. Deferred income tax assets and liabilities are computed for differences between the financial statement and tax bases of assets and liabilities that will result in future taxable or deductible amounts, based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established, when necessary, to reduce deferred income tax assets to the amount expected to be realized.

In accordance with U.S. GAAP, the Company is required to determine whether a tax position of the Company is more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The tax benefit to be recognized is measured as the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. Derecognition of a tax benefit previously recognized could result in the Company recording a tax liability that would reduce net assets. Based on its analysis, the Company has determined that it has not incurred any liability for unrecognized tax benefits as of March 31, 2018 and December 31, 2017. The Company is subject to income tax examinations by major taxing authorities for all tax years since 2013 and its tax returns may be subject to review and adjustment at a later date based on factors including, but not limited to, on-going analyses of and changes to tax laws, regulations and interpretations thereof. No interest expense or penalties have been recognized as of March 31, 2018 and December 31, 2017. During the three months ended March 31, 2018 and 2017, the Company recognized no adjustments for uncertain tax positions.

#### **Stock-Based Compensation**

The Company recognizes expense for its employee stock-based compensation based on the fair value of the awards on the date of grant. The fair values of stock options are estimated on the date of grant using the Black-Scholes option valuation model. The use of the Black-Scholes option valuation model requires the input of subjective assumptions. Compensation cost, net of estimated forfeitures, is recognized ratably over the vesting period of the related stock-based compensation award. For transactions in which goods or services are received from non-employees in return for the issuance of equity instruments, the expense is recognized in the period when the goods and services are received at the fair value of the consideration received or the fair value of the equity instrument issued, whichever is more readily determinable.

#### **New and Recently Adopted Accounting Pronouncements**

In July 2017, the Financial Accounting Standards Board ("FASB") issued Accounting Standard Update ("ASU") No. 2017-11, *Earnings Per Share (Topic 260), Distinguishing Liabilities from Equity (Topic 480), Derivatives and Hedging (Topic 815)*. The amendments in Part I of this update change the classification analysis of certain equity-linked financial instruments (or embedded features) with down round features. When determining whether certain financial instruments should be classified as liabilities or equity instruments, a down round feature no longer precludes equity classification when assessing whether the instrument is indexed to an entity's own stock. The amendments also clarify existing disclosure requirements for equity-classified instruments. As a result, a freestanding equity-linked financial instrument (or embedded conversion option) no longer would be accounted for as a derivative liability at fair value as a result of the existence of a down round feature. This standard is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, with early adoption permitted. The Company is currently evaluating the effect that the new guidance will have on its financial statements and related disclosures.

**FUSION CONNECT, INC. AND SUBSIDIARIES**

In February 2016, the FASB issued ASU No. 2016-02, *Leases*, which is effective for fiscal years, and interim periods within those years, beginning after December 15, 2018 with early adoption permitted. Under ASU 2016-02, lessees will be required to recognize for all leases at the commencement date a lease liability, which is a lessee's obligation to make lease payments arising from a lease measured on a discounted basis, and a right to-use asset, which is an asset that represents the lessee's right to use or control the use of a specified asset for the lease term. The Company is currently evaluating the effect that the new guidance will have on its financial statements and related disclosures.

**Note 3: Discontinued Operations**

On August 26, 2017, the Company and its wholly owned subsidiary, Fusion BCHI Acquisition LLC, a Delaware limited liability company ("Merger Sub"), entered into an Agreement and Plan of Merger (the "Merger Agreement") with Birch Communications Holdings, Inc., a Georgia corporation ("Birch"). As part of this Merger Agreement, the Company is required to spin-off or otherwise exit its Carrier Services business segment prior to the closing of the Merger. See "Note 19 - Subsequent Events." Accordingly, the Company determined that the assets and liabilities of its Carrier Services reportable segment met the discontinued operations criteria in ASC 205-20-45 in the quarter ended March 31, 2018. As such, assets, liabilities and results of operations have been classified as discontinued operations for all periods presented in the accompanying Consolidated Balance Sheet, Consolidated Statements of Operations and Consolidated Statements of Cash Flows.

Summarized operating results for discontinued operations, for the periods ended March 31, 2018 and 2017, respectively, are as follows:

	<b>For the Three Months Ended March 31,</b>	
	<b>2018</b>	<b>2017</b>
<b>Revenues</b>	\$ 9,955,558	\$ 7,330,836
Cost of revenues, exclusive of depreciation and amortization, shown separately below	9,659,011	7,130,207
<b>Gross profit</b>	296,547	200,629
Depreciation and amortization	1,201	1,200
Selling, general and administrative expenses	461,521	521,213
Total operating expenses	462,722	522,413
<b>Operating loss</b>	(166,175)	(321,784)
<b>Other (expenses) income:</b>		
Other (expenses) income, net	-	(39)
Total other expenses	-	(39)
Loss before income taxes	(166,175)	(321,823)
Provision for income taxes	-	-
<b>Net loss</b>	<u>(166,175)</u>	<u>(321,823)</u>

**FUSION CONNECT, INC. AND SUBSIDIARIES**

The carrying amounts of assets and liabilities for discontinued operations for the periods ended March 31, 2018 and December 31, 2017 are as follows:

	<u>March 31, 2018</u>	<u>December 31, 2017</u>
Cash and cash equivalents	\$ 165,165	\$ 57,552
Accounts receivable, net of allowance for doubtful accounts of approximately \$42,000 and \$32,000, respectively	4,099,748	2,328,674
Prepaid expenses and other current assets	4,740	481,727
<b>Total current assets of discontinued operations</b>	<u>4,269,653</u>	<u>2,867,953</u>
Property and equipment, net	16,494	17,695
Security deposits	3,286	3,285
<b>Total non-current assets of discontinued operations</b>	<u>19,780</u>	<u>20,980</u>
Accounts payable and accrued expenses	3,991,463	2,303,122
Related party payable	668,815	790,480
<b>Total current liabilities of discontinued operations</b>	<u>4,660,278</u>	<u>3,093,602</u>
Non-current liabilities	-	-
<b>Total non-current liabilities of discontinued operations</b>	<u>-</u>	<u>-</u>

Operating segments are defined under U.S. GAAP as components of an enterprise for which discrete financial information is available and evaluated regularly by a company's chief operating decision maker in deciding how to allocate resources and assess performance. Prior to the spin-off, the Company had two reportable segments – Business Services and Carrier Services. These segments were organized by the products and services that were sold and the customers that were served. The Company measured and evaluated its reportable segments based on revenues and gross profit margins. Because of a spin-off, Carrier Services are reported as Discontinued Operations and Business Services is the only remaining segment. As a result, segment information is no longer presented in a separate footnote.

**Note 4. Acquisitions**

In January 2018, the Company acquired substantially all of the assets of IQMax, a Charlotte, N.C.-based provider of secure messaging, enterprise data integration and advanced cloud communications solutions. The total consideration for this transaction was \$1.0 million, \$0.5 million of which was paid with 110,124 shares of Fusion common stock, with the remaining portion of the purchase price, also payable in shares of common stock, due six months from the closing date of the transaction. These shares will remain in escrow until 12 months following the closing of the transaction. The Company also agreed to pay a royalty fee to the seller based on the net revenue in excess of \$1.75 million from the annual sales of acquired assets. The estimated present value of the contingent royalty fee of \$0.4 million was recognized as a non-current liability in the condensed consolidated balance sheet as of March 31, 2018.

**FUSION CONNECT, INC. AND SUBSIDIARIES**

The allocation of the purchase price as of the acquisition date is as follows:

		Useful life (in years)
Covenant not to compete	\$ 125,000	3
Trademark	16,125	10
Intellectual property	1,017,805	17
Goodwill	408,069	
Deferred revenue	(119,921)	
Total purchase price	<u>\$ 1,447,078</u>	

**Note 5. Loss per share**

Basic and diluted loss per share is computed by dividing the loss attributable to common stockholders by the weighted-average number of common shares outstanding during the period. The following table sets forth the computation of basic and diluted net loss per share for the three months ended March 31, 2018 and 2017:

	<b>Three Months Ended March 31,</b>	
	<b>2018</b>	<b>2017</b>
<b>Numerator</b>		
Net loss from continuing operations	\$ (4,041,602)	\$ (3,160,125)
Net loss from discontinued operations	(166,175)	(321,823)
Net loss	(4,207,777)	(3,481,948)
Less Net loss attributable to non-controlling interest	66,470	-
Net loss attributable to Fusion Connect, Inc.	(4,141,307)	(3,481,948)
Undeclared dividends on Series A-1, A-2 and A-4 Convertible Preferred Stock	(99,518)	(99,518)
Conversion price reduction on Series B-2 Preferred Stock (see note 14)	-	(623,574)
Series B-2 warrant exchange (see note 14)	-	(347,190)
Dividends declared on Series B-2 Convertible Preferred Stock	(144,064)	(183,827)
Net loss attributable to common stockholders	<u>\$ (4,384,889)</u>	<u>\$ (4,736,057)</u>
<b>Denominator</b>		
Basic and diluted weighted average common shares outstanding	<u>20,682,262</u>	<u>13,805,133</u>
<b>Loss per share basic and diluted</b>		
From continuing operations	<u>\$ (0.20)</u>	<u>\$ (0.32)</u>
From discontinued operations	<u>\$ (0.01)</u>	<u>\$ (0.02)</u>

For the three months ended March 31, 2018 and 2017, the following dilutive securities were excluded from the calculation of diluted earnings per common share because of their anti-dilutive effects:

	<b>For the Three Months Ended March 31,</b>	
	<b>2018</b>	<b>2017</b>
Warrants	1,274,126	1,798,453
Convertible preferred stock	1,265,398	1,375,417
Stock options	1,997,288	1,434,049
	<u>4,536,812</u>	<u>4,607,919</u>

**FUSION CONNECT, INC. AND SUBSIDIARIES**

The net loss per common share calculation includes a provision for preferred stock dividends on Fusion’s outstanding Series A-1, A-2 and A-4 preferred stock (collectively, the “Series A Preferred Stock”) for the three months ended March 31, 2018 and 2017 of \$0.1 million in each period. Through March 31, 2018, the Board of Directors of Fusion has never declared a dividend on any Series A Preferred Stock, resulting in approximately \$5.2 million of accumulated preferred stock dividends. See “Note 19 – Subsequent Events”.

The Fusion Board declared dividends on Fusion Series B-2 Cumulative Convertible Preferred Stock (the “Series B-2 Preferred Stock”) of \$0.1 million and \$0.2 million for the three months ended March 31, 2018 and 2017, respectively. As permitted by the terms of the Series B-2 Preferred Stock, dividends were paid in the form of 3,985 and 71,251 shares of Fusion’s common stock for the three months ended March 31, 2018 and 2017, respectively. See “Note 19 – Subsequent Events”.

**Note 6. Intangible Assets**

Intangible assets as of March 31, 2018 and December 31, 2017 are as follows:

	<u>March 31, 2018</u>			<u>December 31, 2017</u>		
	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Total</u>	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Total</u>
Trademarks and tradename	\$ 1,109,525	\$ (715,166)	\$ 394,359	\$ 1,093,400	\$ (672,314)	\$ 421,086
Proprietary technology	6,798,805	(5,209,277)	1,589,528	5,781,000	(5,005,400)	775,600
Non-compete agreement	12,245,043	(11,758,563)	486,480	12,120,043	(11,701,307)	418,736
Customer relationships	67,614,181	(14,397,003)	53,217,178	67,614,181	(13,073,580)	54,540,601
Favorable lease intangible	-	-	-	218,000	(218,000)	-
Total acquired intangibles	<u>\$ 87,767,554</u>	<u>\$(32,080,009)</u>	<u>\$ 55,687,545</u>	<u>\$ 86,826,624</u>	<u>\$(30,670,601)</u>	<u>\$ 56,156,023</u>

Amortization expense was \$1.6 million and \$2.2 million for the three months ended March 31, 2018 and 2017, respectively. Estimated future aggregate amortization expense is expected to be as follows:

<u>Year</u>	<u>Amortization Expense</u>
remainder of 2018	\$ 4,751,306
2019	5,469,042
2020	5,458,742
2021	5,284,375
2022	4,612,642

**Note 7. Supplemental Disclosure of Cash Flow Information**

Supplemental cash flow information for the three months ended March 31, 2018 and 2017 is as follows:

<u>Supplemental Cash Flow Information</u>	<u>Three Months Ended March 31,</u>	
	<u>2018</u>	<u>2017</u>
Cash paid for interest	<u>\$ 1,961,727</u>	<u>\$ 2,186,314</u>
<b>Supplemental Non-Cash Investing and Financing Activities</b>		
Conversion of preferred stock into common stock	<u>\$ 750,000</u>	<u>\$ 2,958,000</u>
Dividend on Series B-2 preferred stock paid with the issuance of Fusion common stock	<u>\$ 19,479</u>	<u>\$ 183,827</u>
Obligations under acquisition	<u>\$ 500,000</u>	<u>\$ 1,350,000</u>
Common stock issued in acquisition	<u>\$ 500,000</u>	<u>\$ -</u>
Contingent royalty fee	<u>\$ 447,079</u>	<u>\$ -</u>
<b>Reconciliation of Cash, Cash Equivalents and Restricted Cash</b>		
Cash and cash equivalents of continuing operations	<u>\$ 30,999,732</u>	<u>\$ 6,627,115</u>
Restricted cash of continuing operations	<u>27,153</u>	<u>27,153</u>
Total cash, cash equivalents and restricted cash of continuing operations	<u>\$ 31,026,885</u>	<u>\$ 6,654,268</u>
Cash and cash equivalents of discontinued operations	<u>165,165</u>	<u>15,038</u>
Total cash, cash equivalents and restricted cash	<u>\$ 31,192,050</u>	<u>\$ 6,669,306</u>

**FUSION CONNECT, INC. AND SUBSIDIARIES**

**Note 8. Prepaid Expenses and Other Current Assets**

Prepaid expenses and other current assets at March 31, 2018 and December 31, 2017 are as follows:

	<b>March 31, 2018</b>	<b>December 31, 2017</b>
Insurance	\$ 69,355	\$ 18,639
Rent	16,326	16,326
Marketing	157,162	55,801
Software subscriptions	646,495	610,191
Comissions	58,833	46,755
Line costs	391,211	335,978
Other	531,801	525,828
<b>Total</b>	<b><u>\$ 1,871,183</u></b>	<b><u>\$ 1,609,518</u></b>

**Note 9. Accounts Payable and Accrued Expenses**

Accounts payable and accrued expenses at March 31 2018 and December 31, 2017 are as follows:

	<b>March 31, 2018</b>	<b>December 31, 2017</b>
Trade accounts payable	\$ 6,060,192	\$ 7,434,257
Accrued license fees	2,673,648	2,881,331
Accrued sales and federal excise taxes	3,598,141	3,496,697
Deferred revenue	1,517,100	1,283,969
Accrued network costs	1,808,853	1,796,302
Accrued sales commissions	956,150	911,192
Property and other taxes	746,309	759,770
Accrued payroll and vacation	487,711	422,097
Customer deposits	393,868	383,032
Interest payable	7,263	7,263
Credit card payable	135,433	114,209
Accrued USF fees	1,195,512	728,826
Accrued bonus	131,593	333,337
Professional and consulting fees	204,081	171,163
Rent	217,036	163,030
Other	32,555	1,108,968
<b>Total</b>	<b><u>\$ 20,165,445</u></b>	<b><u>\$ 21,995,443</u></b>

**FUSION CONNECT, INC. AND SUBSIDIARIES**

**Note 10. Equipment Financing Obligations**

From time to time, the Company enters into equipment financing or capital lease arrangements to finance the purchase of network hardware and software utilized in its operations. These arrangements require monthly payments over a period of 24 to 48 months with interest rates ranging between 5.3% and 6.6% per annum. The Company's equipment financing obligations are as follows:

	March 31, 2018	December 31, 2017
Equipment financing obligations	\$ 1,482,597	\$ 1,797,374
Less current portion	(1,075,252)	(1,206,773)
Long-term portion	<u>\$ 407,345</u>	<u>\$ 590,601</u>

The Company's payment obligations under its capital leases are as follows:

Year ending December 31:	Principal
remainder of 2018	\$ 891,996
2019	502,589
2020	88,012
	<u>\$ 1,482,597</u>

**Note 11. Long-Term Debt**

**Secured Credit Facilities**

As of March 31, 2018 and December 31, 2017, secured credit facilities consists of the following:

	March 31, 2018	December 31, 2017
Term loan	\$ 55,125,000	\$ 61,750,000
Less:		
Deferred financing fees	(961,758)	(1,027,332)
Current portion	(6,500,000)	(6,500,000)
Term loan - long-term portion	<u>\$ 47,663,242</u>	<u>\$ 54,222,668</u>
Indebtedness under revolving credit facility	<u>\$ -</u>	<u>\$ 1,500,000</u>

On November 14, 2016, Fusion NBS Acquisition Corp. ("FNAC"), a wholly-owned subsidiary of Fusion, entered into a credit agreement (the "East West Credit Agreement") with East West Bank ("EWB"), as administrative agent and the lenders identified therein (collectively the "East West Lenders"). Under the East West Credit Agreement, the East West Lenders extended FNAC (i) a \$65.0 million term loan and (ii) a \$5.0 million revolving credit facility (which includes up to \$4 million in "swingline" loans that may be accessed on a short-term basis).

Borrowings under the East West Credit Agreement are evidenced by notes bearing interest at rates computed based upon either the then current "prime" rate of interest or "LIBOR" rate of interest, as selected by FNAC. Interest on borrowings that FNAC designates as "base rate" loans bear interest at the greater of the prime rate published by the Wall Street Journal or 3.25% per annum, in each case plus 2% per annum. Interest on borrowings that FNAC designates as "LIBOR rate" loans bear interest at the LIBOR rate of interest published by the Wall Street Journal, plus 5% per annum. The current interest rate is 6.75% per annum.

Effective January 1, 2018, the Company is required to make monthly principal payments in the amount of \$541,667 until the November 12, 2021 maturity date of the term loan, when the remaining \$36.8 million of principal is due. Borrowings under the revolving credit facility are also payable on the November 12, 2021 maturity date of the facility. At March 31, 2018 and December 31, 2017, \$0 and \$1.5 million, respectively, was outstanding under the revolving credit facility.

## FUSION CONNECT, INC. AND SUBSIDIARIES

Under the East West Credit Agreement:

- The Company is subject to a number of affirmative and negative covenants, including but not limited to, restrictions on paying indebtedness subordinate to its obligations to the East West Lenders, incurring additional indebtedness, making capital expenditures, dividend payments and cash distributions by subsidiaries.
- The Company is required to comply with various financial covenants, including leverage ratio, fixed charge coverage ratio and minimum levels of earnings before interest, taxes, depreciation and amortization; and its failure to comply with any of the restrictive or financial covenants could result in an event of default and accelerated demand for repayment of amounts outstanding.
- The Company granted the lenders security interests on all of its assets, as well as its membership interest in FGS and the capital stock of FNAC and each of its subsidiaries.
- Fusion and its subsidiaries (and future subsidiaries of both) other than FNAC and FGS have guaranteed FNAC's obligations, including FNAC's repayment obligations thereunder.

At March 31, 2018 and December 31, 2017, the Company was in compliance with all of the financial covenants contained in the East West Credit Agreement. See "Note 19 – Subsequent Events".

### *Notes Payable – Non-Related Parties*

At March 31, 2018 and December 31, 2017, notes payable – non-related parties consists of the following:

	<b>March 31, 2018</b>	<b>December 31, 2017</b>
Subordinated notes	\$ 33,588,717	\$ 33,588,717
Discount on subordinated notes	(958,052)	(1,040,167)
Deferred financing fees	(547,111)	(595,387)
Total notes payable - non-related parties	32,083,554	31,953,163
Less: current portion	-	-
Long-term portion	\$ 32,083,554	\$ 31,953,163

On November 14, 2016, FNAC, Fusion and Fusion's other subsidiaries entered into the Fifth Amended and Restated Securities Purchase Agreement (the "Praesidian Facility") with Praesidian Capital Opportunity Fund III, L.P., Praesidian Capital Opportunity Fund III-A, LP and United Insurance Company of America (collectively, the "Praesidian Lenders"). The Praesidian Facility amends and restates a prior facility, pursuant to which FNAC previously sold its Series A, Series B, Series C, Series D, Series E and Series F senior notes in an aggregate principal amount of \$33.6 million (the "SPA Notes"). These notes require interest payments in the amount of \$0.3 million per month. The current interest rate is 10.8% per annum.

Under the terms of the Praesidian Facility, the maturity date of the SPA Notes is May 12, 2022, no payments of principal are due until the maturity date, and the financial covenants contained in the Praesidian Facility are substantially similar to those contained in the East West Credit Agreement. In connection with the execution of the Praesidian Facility, the Praesidian Lenders entered into a subordination agreement with the East West Lenders pursuant to which the Praesidian Lenders have subordinated their right to payment under the Praesidian Facility and the SPA Notes to repayment of the Company's obligations under the East West Credit Agreement. At March 31, 2018 and December 31, 2017, the Company was in compliance with all of the financial covenants contained in the Praesidian Facility. See "Note 19 – Subsequent Events".

**Notes Payable – Related Parties**

At March 31, 2018 and December 31, 2017, the Company had \$0.9 million of outstanding notes payable due to Marvin Rosen, the Chairman of Fusion’s Board of Directors. These notes are subordinated to borrowings under the East West Credit Agreement and the Praesidian Facility. The notes are unsecured, pay interest monthly at an annual rate of 7%, and mature 120 days after the Company’s obligations under the East West Credit Agreement and the Praesidian Facility are paid in full. See “Note 19 – Subsequent Events”.

**Note 12. Obligations Under Asset Purchase Agreements**

In connection with certain acquisitions and asset purchases completed by the Company during 2016, 2017 and 2018, the Company has various obligations to the sellers, mainly for payments of portions of the purchase price that have been deferred under the terms of the respective asset purchase agreements. Such obligations to sellers or other parties associated with these transactions as of March 31, 2018 and December 31, 2017 are as follows:

	March 31, 2018	December 31, 2017
Customer base acquisitions	\$ 253,380	\$ 450,000
IQMax	947,079	-
	<u>1,200,459</u>	<u>450,000</u>
Less current portion	(723,297)	(227,760)
Long-term portion	<u>\$ 477,162</u>	<u>\$ 222,240</u>

**Note 13. Derivative Liability**

Fusion has issued warrants to purchase shares of its common stock in connection with certain debt and equity financing transactions. These warrants are accounted for in accordance with the guidance contained in *ASC Topic 815, Derivatives and Hedging*. For warrant instruments that are not deemed to be indexed to Fusion’s common stock, the Company classifies such instruments as a liability at its fair value and adjusts the instrument to fair value at each reporting period. This liability is subject to re-measurement at each balance sheet date until the warrant is exercised or expires, and any change in fair value is recognized in the Company’s statement of operations. At March 31, 2018, Fusion had 203,647 warrants outstanding which provide for a downward adjustment of the exercise price if Fusion were to issue common stock at an issuance price, or issue convertible debt or warrants with a conversion or exercise price, that is less than the exercise price of these warrants. During the three months ended March 31, 2018, 37,120 warrants were exercised, resulting in a reclassification to equity in the amount of \$0.1 million. During the three months ended March 31, 2017, 12,800 of these warrants were exercised, and \$13,000 was reclassified from the Company’s derivative liability into equity.

The fair values of these warrants have been estimated using option pricing and other valuation models, and the quoted market price of Fusion common stock. The following weighted average assumptions were used to determine the fair value of the warrants for the three months ended March 31, 2018 and 2017:

	Three months ended March 31,	
	2018	2017
Stock price (\$)	4.85	2.37
Adjusted Exercise price (\$)	2.34	2.34
Risk-free interest rate (%)	2.09	2.23
Expected volatility (%)	86.90	74.40
Time to maturity (years)	1.00	1.75

At March 31, 2018 and December 31, 2017, the fair value of the derivative was \$0.6 million and \$0.9 million, respectively. For the three months ended March 31, 2018, the Company recognized a gain on the change in fair value of the derivative of \$0.2 million, and for the three months ended March 31, 2017, the Company recognized a loss on the change in fair value of the derivative in the amount of \$40,000.

**Note 14. Revenues from Contracts with Customers**

In May 2014, the FASB issued ASU 2014-09, *Revenues from Contracts with Customers (Topic 606)* (“ASU 2014-09”), as subsequently amended, that outlines a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most recent revenue recognition guidance, including industry-specific guidance. The core principle of the revenue model is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This standard is effective for public companies for years ending after December 15, 2017, with early adoption permitted. In March 2016, April 2016 and December 2016, the FASB issued ASU No. 2016-08, *Revenue From Contracts with Customers (ASC 606): Principal Versus Agent Considerations*, ASU No. 2016-10, *Revenue From Contracts with Customers: Identifying Performance Obligations and Licensing*, and ASU No. 2016-20, *Technical Corrections and Improvements to Topic 606, Revenue From Contracts with Customers*, respectively, which further clarify the implementation guidance on principal versus agent considerations contained in ASU No. 2014-09. In May 2016, the FASB issued ASU 2016-12, *Revenue from Contracts with Customers, narrow-scope improvements and practical expedients* which provides clarification on assessing the collectability criterion, presentation of sales taxes, measurement date for non-cash consideration and completed contracts at transition. These standards became effective for the Company beginning with the first quarter of 2018.

## FUSION CONNECT, INC. AND SUBSIDIARIES

The Company adopted ASC 606 using the modified retrospective method by recognizing the cumulative effect of initially applying ASC 606 as an adjustment to the opening balance of shareholders' equity at January 1, 2018. The historical periods have not been adjusted and continue to be reported under ASC 605 "Revenue Recognition".

The following table includes information for the transition adjustment recorded as of January 1, 2018 to record the cumulative impact of adoption of ASC 606:

	Balance as of December 31, 2017	ASC 606 Transition Adjustment	Balance as of January 1, 2018
<b>Assets</b>			
Deferred installation costs, current	\$ -	\$ 783,667	\$ 783,667
Deferred installation costs, non-current	-	1,125,414	1,125,414
	-	1,909,081	1,909,081
<b>Liabilities</b>			
Deferred installation revenue, current	-	(785,740)	(785,740)
Deferred installation revenue, non-current	-	(1,036,657)	(1,036,657)
	-	(1,822,397)	(1,822,397)
<b>Stockholders' Equity</b>			
Accumulated deficit	\$ -	\$ 86,684	\$ 86,684

Under this new guidance, the Company recognizes revenue when its customer obtains control of promised services, in an amount that reflects the consideration which the Company expects to receive in exchange for those services. To determine whether arrangements are within the scope of this new guidance, the Company performs the following five steps: (i) identifies the contract with a customer; (ii) identifies the performance obligations in the contract; (iii) determines the transaction price; (iv) allocates the transaction price to the performance obligations in the contract; and (v) recognizes revenue when (or as) the Company satisfies its performance obligation. The details of changes under the new guidance are as follow:

### Contract Acquisition Costs

Under ASC 606, certain costs to acquire customers must be deferred and amortized over the related contract period of expected customer life. For the Company, this includes certain commissions paid to acquire new customers. Beginning January 1, 2018, commissions attributable to new customer contracts are being deferred and amortized into expense. Historically, these acquisition costs were expensed as incurred. The Company determined that incremental commissions paid as a result of acquiring customers are recoverable and, therefore, as part of the transition adjustment above, current deferred installation costs of \$784,000 and non-current deferred installation costs of \$1,125,000 were capitalized. For the three months ended March 31, 2018, the Company capitalized a total of \$209,000 and amortized \$217,000 of commissions. As of March 31, 2018, the Company recorded a total of \$798,000 of current deferred installation costs and \$1,103,000 of non-current deferred installation costs in its consolidated balance sheet.

### Installation Revenues

Under ASC 606, certain installation fees charged to the customers did not represent separate performance obligations and, as a result, these fees must be deferred and recognized over the related contract period of expected customer life. Beginning January 1, 2018, installation revenues attributable to the customer contracts are being deferred and amortized into revenue. Historically, these revenues were recognized when completed. As part of the transition adjustment above, the Company recorded a total of \$786,000 of current deferred installation revenue and \$1,036,000 of non-current deferred installation revenue at January 1, 2018. For the three months ended March 31, 2018, the Company deferred a total of \$225,000 and recognized \$221,000 of installation revenue. As of March 31, 2018, the Company recorded a total of \$797,000 of current deferred installation revenue and \$1,029,000 of non-current deferred installation revenue on our consolidated balance sheet.

The following table summarize the impacts of adopting ASC 606 on Company's consolidated balance sheet and statement of operations as of and for the three months ended March 31, 2018:

FUSION CONNECT, INC. AND SUBSIDIARIES

	March 31, 2018		
	As reported	Previous guidance	Impact of Adoption of ASC 606
<b>Assets</b>			
Deferred installation costs, current	\$ 798,166	\$ -	\$ 798,166
Deferred installation costs, non-current	1,102,648	-	1,102,648
	<u>1,900,814</u>	-	<u>1,900,814</u>
<b>Liabilities</b>			
Deferred installation revenue, current	(797,332)	-	\$ (797,332)
Deferred installation revenue, non-current	(1,029,445)	-	(1,029,445)
	<u>(1,826,777)</u>	-	<u>(1,826,777)</u>
<b>Stockholders' Equity</b>			
Accumulated deficit	<u>\$201,318,706</u>	<u>\$201,244,669</u>	<u>\$ (74,037)</u>

	For the three months ended March 31, 2018		
	As reported	Previous guidance	Impact of Adoption of ASC 606
Revenues	\$ 29,038,043	\$ 29,042,422	\$ (4,379)
Selling, general and administrative	(13,947,995)	(13,939,728)	(8,267)
Net Impact	<u>\$ 15,090,048</u>	<u>\$ 15,102,694</u>	<u>\$ (12,646)</u>

The impact of adoption of ASC 606 on net income, basic and diluted net loss per share, consolidated statement of operations and the consolidated statement of cash flows were not material for the three months ended March 31, 2018.

The following table includes estimated revenue expected to be recognized in the future related to performance obligations that are unsatisfied (or partially unsatisfied) at the end of the reporting period:

	Deferred installation revenue	Deferred installation costs	Net
2018 (remaining nine months)	\$ 616,688	\$ (614,571)	\$ 2,117
2019	634,105	(663,614)	(29,509)
2020	405,576	(459,859)	(54,283)
2021 and thereafter	170,408	(162,770)	7,638
	<u>\$ 1,826,777</u>	<u>\$ (1,900,814)</u>	<u>\$ (74,037)</u>

Summary of disaggregated revenue for the three months periods ended March 31, 2018 and 2017 is as follows:

Revenue category	For the three months ended March 31, 2018			For the three months ended March 31, 2017
	As reported	Previous guidance	Impact of Adoption of ASC 606	
Monthly recurring	\$ 24,313,686	\$ 24,313,686	\$ -	24,721,490
Usage and other	4,473,467	4,473,467	-	3,444,654
Installation	250,890	255,269	(4,379)	314,895
Total revenue	<u>\$ 29,038,043</u>	<u>\$ 29,042,422</u>	<u>\$ (4,379)</u>	<u>\$ 28,481,039</u>

**Note 15. Equity Transactions**

**Common Stock**

Fusion is authorized to issue 150,000,000 shares of common stock. As of March 31, 2018 and December 31, 2017, 23,847,140 and 14,980,756 shares of its common stock, respectively, were issued and outstanding. See "Note 19 – Subsequent Events".

In February 2018, the Company completed an underwritten public offering whereby Fusion issued 8,625,000 shares of its common stock and received net proceeds of \$38.2 million. The proceeds from this offering are being used to pay down certain indebtedness and for general corporate purposes.

## FUSION CONNECT, INC. AND SUBSIDIARIES

During the three months ended March 31, 2018, Fusion issued 27,275 shares of common stock upon the exercise of outstanding warrants, and declared dividends of \$144,000 on the Series B-2 Preferred Stock, which was paid in the form of 3,985 shares of Fusion common stock.

In March 2017, the Company entered into exchange agreements with certain holders of its outstanding warrants whereby the outstanding warrants were exchanged for new warrants (the "2017 Warrants"), which warrants permitted the holders to exercise and purchase, for a limited period of 60 days, unregistered shares of Fusion common stock at a discount of up to 10% below the closing bid price of the common stock at the time of exercise but in no event at a price of less than \$1.95 per share. In connection with these exchange agreements, the warrant holders exercised warrants to purchase 374,556 shares of common stock on March 31, 2017 at an exercise price of \$2.09 per share. The Company received proceeds from the exercise of the 2017 Warrants in the amount of \$0.8 million, which will be used for general corporate purposes. All of the 2017 Warrants were immediately exercised and none remained outstanding as of March 31, 2017. As a result of the exchange, the Company recorded a preferred stock dividend in the amount of \$0.3 million for the difference in fair value of the warrants that were exchanged (see note 5).

### Preferred Stock

Fusion is authorized to issue up to 10,000,000 shares of preferred stock. As of March 31, 2018 and December 31, 2017, there were 5,045 shares of Series A Preferred Stock issued and outstanding. In addition, there were 8,421 and 9,171 shares of Series B-2 Preferred Stock issued and outstanding as of March 31, 2018 and December 31, 2017, respectively. See "Note 19 – Subsequent Events".

During the three months ended March 31, 2018, 750 shares of Series B-2 Preferred stock were converted into 100,000 shares of Fusion common stock.

On March 31, 2017, the Company agreed with certain holders of its Series B-2 Preferred Stock to convert their shares of Series B-2 Preferred Stock into shares of Fusion common stock at a conversion price of \$4.50 per share (a three dollar reduction from the specified conversion price). As a result, 2,958 shares of Series B-2 Preferred Stock were converted into a total of 657,777 shares of Fusion common stock, and the Company recorded a preferred stock dividend of \$0.6 million for the value of the incremental number of common shares issued in connection with the reduction in the conversion price of the Series B-2 Preferred Stock (see note 5).

The holders of the Series A Preferred Stock are entitled to receive cumulative dividends of 8% per annum payable in arrears, when and if declared by Fusion's Board, on January 1 of each year. As of March 31, 2018, no dividends have been declared with respect to the Series A Preferred Stock (see note 5). The holders of the Series B-2 Preferred Stock are entitled to receive cumulative dividend of 6% per annum payable quarterly in arrears when and if declared by Fusion's Board, in cash or shares of Fusion common stock, at the option of the Company (see note 5).

### Stock Options

Fusion's 2016 equity incentive plan reserves a number of shares of common stock equal to 10% of Fusion common stock outstanding from time to time on a fully diluted basis, adjusted upward for the number of shares available for grant under Fusion's 2009 stock option plan plus the number of shares covered by options granted under the 2009 plan that expire without being exercised. The 2016 equity incentive plan provides for the grant of incentive stock options, stock appreciation rights, restricted stock, restricted stock units, stock grants, stock units, performance shares and performance share units to employees, officers, non-employee directors of, and consultants to the Company. Options issued under the various Fusion plans typically vest in annual increments over a three or four year period, expire ten years from the date of grant and are issued at exercise prices no less than 100% of the fair market value at the time of grant.

The following assumptions were used to determine the fair value of the stock options granted under Fusion's stock-based compensation plans using the Black-Scholes option-pricing model:

	Three Months Ended March 31,	
	2018	2017
Dividend yield	0.0%	0.0%
Expected volatility	92.40%	92.40%
Average Risk-free interest rate	2.56%	2.27%
Expected life of stock option term (years)	8.00	8.00

## FUSION CONNECT, INC. AND SUBSIDIARIES

The Company recognized compensation expense of \$0.4 million and \$0.2 million for the three months ended March 31, 2018 and 2017, respectively. These amounts are included in selling, general and administrative expenses in the condensed consolidated interim statements of operations.

The following table summarizes stock option activity for the three months ended March 31, 2018:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contract Term
Outstanding at December 31, 2017	2,011,952	\$ 3.57	
Granted	4,800	5.48	
Exercised	-	-	
Forfeited	(1,500)	2.55	
Expired	(17,964)	14.57	
Outstanding at March 31, 2018	<u>1,997,288</u>	3.48	8.09
Exercisable at March 31, 2018	<u>1,416,765</u>	4.04	7.92

As of March 31, 2018, the Company had approximately \$0.9 million of unrecognized compensation expense related to stock options granted under the Company's stock-based compensation plans, which is expected to be recognized over a weighted-average period of 1.7 years.

### Note 16. Commitments and Contingencies

From time to time, the Company may be involved in a variety of claims, lawsuits, investigations and proceedings relating to contractual disputes, employment matters, regulatory and compliance matters, intellectual property rights and other litigation arising in the ordinary course of business. Defending such proceedings can be costly and can impose a significant burden on management and employees. As of March 31, 2018, the Company does not expect that the outcome of any such claims or actions will have a material adverse effect on the Company's liquidity, results of operations or financial condition.

The Company underwent a compliance audit for the use of certain software licenses by one of the Company's recently acquired businesses. The Company is negotiating with the software vendor with regard to a settlement and based upon correspondence and conversations with the vendor, the Company has recorded an accrual in accounts payable and accrued expenses in the accompanying consolidated balance sheet. There can be no assurances that this matter will be settled and, if settled, the amount that we would pay in any such settlement.

### Note 17. Related Party Transactions

Since March 6, 2014, the Company has engaged a tax advisor to prepare its tax returns and to provide related tax advisory services. The Company was billed \$0 and \$0.1 million for the three months ended March 31, 2018 and 2017, respectively, by this firm. Larry Blum, a member of Fusion's Board of Directors, is a Senior Advisor to, and a former partner of, this firm.

The Company has also issued notes payable to Marvin Rosen (see note 10). See "Note 19 – Subsequent Events".

### Note 18. Fair Value Disclosures

Fair value of financial and non-financial assets and liabilities is defined as an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. The three-tier hierarchy for inputs used in measuring fair value, which prioritizes the inputs used in the methodologies of measuring fair value for assets and liabilities, is as follows:

**FUSION CONNECT, INC. AND SUBSIDIARIES**

Level 1—Quoted prices in active markets for identical assets or liabilities

Level 2—Observable inputs other than quoted prices in active markets for identical assets and liabilities

Level 3—No observable pricing inputs in the market

The following table represents the liabilities measured at fair value on a recurring basis:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>	<u>Total</u>
<b>As of March 31, 2018</b>				
Current liabilities:				
Contingent purchase price liability	-	-	\$ 223,297	\$ 223,297
Non-current liabilities:				
Contingent purchase price liability	-	-	\$ 477,162	\$ 477,162
Derivative liability (see note 13)	-	-	\$ 586,197	\$ 586,197
<b>As of December 31, 2017</b>				
Current liabilities:				
Contingent purchase price liability	-	-	\$ 227,760	\$ 227,760
Non-current liabilities:				
Contingent purchase price liability	-	-	\$ 222,240	\$ 222,240
Derivative liability (see note 13)	-	-	\$ 872,900	\$ 872,900

Changes in the derivative warrant liability for the three months ended March 31, 2018 are as follows:

Balance at December 31, 2017	\$ 872,900
Change for the period:	
Change in fair value included in net loss	(194,312)
Warrant exercises (see note 13)	(92,391)
Balance at March 31, 2018	<u>\$ 586,197</u>

**Note 19. Subsequent Events**

***Completion of the Acquisition of Birch Communications***

On May 4, 2018 (the “Closing Date”), Fusion completed the various transactions contemplated by the Merger Agreement. As contemplated by the Merger Agreement, on the Closing Date, Birch merged with and into Merger Sub, with Merger Sub surviving the merger as a wholly-owned subsidiary of Fusion.

On the Closing Date, all of the outstanding shares of common stock, par value \$0.01 per share, of Birch (other than treasury shares or shares owned of record by any Birch subsidiary) were cancelled and converted into the right to receive, in the aggregate, 49,896,310 shares (the “Merger Shares”) of Fusion Common Stock. Pursuant to subscription agreements executed by each of the shareholders of Birch, the Merger Shares were issued in the name of, and are now held by, BCHI Holdings, LLC, a Georgia limited liability company owned by the former shareholders of Birch.

***Carrier Spin-Off***

On the Closing Date, Fusion entered into a Membership Interest Purchase and Sale Agreement (the “Membership Sale Agreement”) with XComIP pursuant to which Fusion transferred its sixty percent (60%) membership interest in FGS to XComIP in exchange for a right to receive: (i) sixty percent (60%) of the Net Profits (as defined in the Membership Sale Agreement) of FGS; (ii) sixty percent (60%) of any distributions being made by FGS to its members only to the extent such amounts are not distributed as part of the distribution of Net Profits; and (iii) sixty percent (60%) of the net proceeds received by the members from a sale of FGS to a third party.

*Senior Secured Credit Facilities*

On the Closing Date, Fusion entered into a First Lien Credit and Guaranty Agreement (the “First Lien Credit Agreement”) with Wilmington Trust, National Association, as Administrative Agent and Collateral Agent (in such capacities, the “First Lien Agent”), the lenders party thereto (the “First Lien Lenders”), and all of the U.S.-based subsidiaries of Fusion, as guarantors thereunder (the “Guarantors”), pursuant to which the First Lien Lenders extended (a) term loans to Fusion in an aggregate principal amount of \$555,000,000, consisting of the “Tranche A Term Loan” and “Tranche B Term Loan,” in an aggregate principal amount of \$45,000,000 and \$510,000,000, respectively (collectively, the “First Lien Term Loan”), and (b) a revolving facility in an aggregate principal amount of \$40,000,000 (the “Revolving Facility”, and together with the First Lien Term Loan, the “First Lien Facility”). Borrowings under the First Lien Credit Agreement are computed based upon either the then current “base rate” of interest or “LIBOR” rate of interest, as selected by Fusion at the time of its borrowings. The Tranche A Term Loan has an original issue discount of 0.5%. The Tranche B Term Loan has an original issue discount of 4%, except for the \$170 million portion of the Tranche B Term Loan made by one lender and certain of its affiliates, which has an original issue discount of 9%, for a blended original issue discount of approximately 5.67%. The Tranche A Term Loan and the Revolving Facility mature on the fourth anniversary of the Closing Date and the Tranche B Term Loan matures on the fifth anniversary of the Closing Date. The Guarantors guaranty the obligations of Fusion under the First Lien Credit Agreement.

In addition, Fusion simultaneously entered into a Second Lien Credit and Guaranty Agreement (the “Second Lien Credit Agreement”, and with the First Lien Credit Agreement, the “Credit Agreements”), by and among Fusion, the Guarantors, Wilmington Trust, National Association, as Administrative Agent and Collateral Agent (in such capacities, the “Second Lien Agent”, and together with the First Lien Agent, collectively the “Agents”), and the lenders party thereto (the “Second Lien Lenders”, and together with the First Lien Lenders, the “Lenders”), pursuant to which the Second Lien Lenders extended a term loan in the aggregate principal amount of \$85,000,000 (the “Second Lien Term Loan”, and collectively with the First Lien Term Loan, the “Term Loans”, and collectively with the First Lien Facility, the “Credit Facilities”). Borrowings under the Second Lien Credit Agreement are computed based upon either the then current “base” rate of interest or “LIBOR” rate of interest, as selected by Fusion at the time of its borrowings. The Second Lien Term Loan has an original issue discount of 4.00%, and it matures 5.5 years from the Closing Date. The Guarantors guaranty the obligations of Fusion under the Second Lien Credit Agreement. The Credit Facilities may be prepaid, in whole or in part, subject to specified prepayment premiums.

Under the Credit Agreements, Fusion is subject to a number of affirmative and negative covenants, including but not limited to, restrictions on paying indebtedness subordinate to its obligations to the Lenders, incurring additional indebtedness, making capital expenditures, dividend payments and cash distributions by subsidiaries. Furthermore, Fusion is required to comply with various financial covenants, including net leverage ratio, fixed charge coverage ratio and maximum levels of consolidated capital expenditures; and its failure to comply with any of the restrictive or financial covenants could result in an event of default and accelerated demand for repayment of its indebtedness.

The proceeds of the Term Loans have been used, in part, to refinance all of the existing indebtedness of Fusion and its subsidiaries (including Birch), under (i) the East West Bank Credit Agreement; (ii) the Praesidian Facility; and (iii) the Credit Agreement, dated as of July 18, 2014, among Birch Communications Holdings, Inc., Birch Communications, Inc., Cbeyond, Inc., the other guarantors party thereto, the lenders party thereto and PNC Bank, National Association, as Administrative Agent. In addition, the Term Loans were used to repay, in full, approximately \$929,000 of indebtedness under that certain Second Amended and Restated Unsecured Promissory Note, dated November 14, 2016, payable by Fusion to Marvin Rosen. The proceeds were also be used to pay the fees and expenses associated with the Birch Merger and related transactions, including in connection with the Credit Facilities.

The Term Loans were also used to make a prepayment of an aggregate of approximately \$3.0 million of indebtedness of Birch under the subordinated notes each dated October 28, 2016, in favor of Holcombe T. Green, Jr., R. Kirby Godsey and the Holcombe T. Green, Jr. 2013 Five-Year Annuity Trust. The remaining indebtedness thereunder is evidenced after the closing of the Birch Merger by Amended and Restated Subordinated Notes, dated as of the Closing Date, made by BCHI Merger Sub (as successor in interest to Birch pursuant to the Birch Merger) with an aggregate principal amount of \$3.3 million (the “Bircan Notes”). The Bircan Notes each have an interest rate of 12% per annum, and are amortized in three equal installments, to be paid off completely in March 2019, with interest due in quarterly installments. The indebtedness under the Bircan Notes is unsecured, and obligations thereunder are subordinated to the Credit Facilities.

In addition, \$62,000,000 of the Tranche B Term Loan under the First Lien Credit Agreement has been deposited in a deposit account with EWB, which account is subject to the terms of a deposit account control agreement by and among Fusion, EWB, and the First Lien Agent. The amounts deposited in this account will be used by Fusion to pay the Purchase Price (as defined below) for MegaPath Holdings Corporation (“MegaPath”). If the MegaPath Merger (as defined below) is not completed by August 4, 2018, such funds must be used to prepay the Tranche B Term Loan under the First Lien Credit Agreement.

***Green Subordinated Note***

At Closing, Holcombe T. Green, Jr. made an additional loan to Fusion in the principal amount of \$10,000,000, which is evidenced by a Subordinated Promissory Note, dated the Closing Date (the “Green Note”), that Fusion delivered to Mr. Green. The Green Note has an interest rate of 13% per annum and an original issue discount of 4%, and it matures on the date which is 91 days after the maturity date of the Second Lien Term Loan. Until the maturity date of the Green Note, only interest is due thereunder, in quarterly payments. The indebtedness under the Green Note is unsecured, and obligations thereunder are subordinated to the Credit Facilities.

***Vector Subordinated Note***

In connection with its participation in the Tranche B Term Loan under the First Lien Credit Agreement, Vector Fusion Holdings (Cayman), Ltd. (“Vector”) entered into a separate credit agreement (the “Vector Credit Agreement”) with Goldman Sachs & Co., as administrative agent and lender, and U.S. Bank National Association, as collateral agent and collateral custodian, pursuant to which Vector borrowed funds from Goldman Sachs, the proceeds of which were used to purchase Tranche B Term Loans under the First Lien Credit Agreement. In connection therewith, Vector issued to Fusion, and Fusion bought from Vector using proceeds of the various financing transactions consummated on the Closing Date, a \$25,000,000 unsecured subordinated note (the “Vector Note”). The Vector Note bears interest at the rate earned by the bank account in which the proceeds of the Vector Note will be deposited and matures on May 3, 2024. The Vector Note is subordinate in right of payment to Vector’s loan from Goldman Sachs & Co. Other than payments permitted under certain limited circumstances set forth in the Vector Credit Agreement, Fusion is not entitled to any distribution on account of the principal, premium or interest or any other amount in respect of the Vector Note until all amounts owed by Vector under the Vector Credit Agreement are paid in full. Similarly, while Fusion has the right to declare obligations due under the Vector Note to be immediately due and payable upon the occurrence of an event of default (including, without limitation, in the event of any insolvency, bankruptcy or liquidation or Vector), Fusion will not be entitled to receive any payment on account of the Vector Note until Vector’s obligations under the Senior Credit Agreement are paid in full. Fusion pledged the Vector Note as security for its obligations under the Credit Agreements.

***Private Placements of Common Stock***

On the Closing Date, Fusion entered into and consummated the sale of shares of Fusion common stock under three separate common stock purchase agreements. Specifically, Fusion issued and sold (i) 952,382 shares of Fusion common stock, for an aggregate purchase price of approximately \$5,000,000, to North Haven Credit Partners II L.P., one of the First Lien Lenders under the Tranche B Term Loan, which is managed by Morgan Stanley Credit Partners; (ii) 380,953 shares of Fusion common stock, for an aggregate purchase price of approximately \$2,000,000, to Aetna Life Insurance Company; and (iii) 190,477 shares of Fusion common stock, for an aggregate purchase price of approximately \$1,000,000, to Backcast Credit Opportunities Fund I, L.P. These shares of common stock were sold in reliance upon the exemption from the registration requirements under the Securities Act of 1933, as amended (“Securities Act”) pursuant to Section 4(a) (2) thereunder.

***Private Placement of Series D Preferred Stock***

On the Closing Date, Fusion entered into a preferred stock purchase agreement with Holcombe T. Green, Jr. pursuant to which it issued and sold to Mr. Green 15,000 shares of Series D Cumulative Preferred Stock, par value \$0.01 per share (the “Series D Preferred Stock”) of Fusion, for an aggregate purchase price of \$14,700,000. The Series D Preferred Stock has a stated value of \$15,000,000. The Series D Preferred Shares were sold in reliance upon the exemptions from the registration requirements under the Securities Act pursuant to Section 4(a)(2) thereunder. The Series D Preferred Stock accrues dividends when, as and if declared by the Fusion Board at an annual rate of twelve percent (12%) per annum, payable monthly in arrears on a cumulative basis.

***MegaPath Merger Agreement***

On May 4, 2018, Fusion, and its wholly owned subsidiary, Fusion MPHC Acquisition Corp., a Delaware corporation (“MPHC Merger Sub”), entered into an Agreement and Plan of Merger (the “MegaPath Merger Agreement”), with MegaPath and Shareholder Representative Services LLC, a Colorado limited liability company, solely in its capacity as the representative of the stockholders and optionholders of MegaPath. The MegaPath Merger Agreement, provides, among other things, that upon the terms and conditions set forth therein, MPHC Merger Sub will merge with and into MPHC Merger Sub, with MegaPath surviving the MegaPath Merger and continuing as a wholly-owned subsidiary of Fusion. The purchase price for MegaPath is \$71,500,000 (the “Purchase Price”), up to \$10,000,000 of which may be paid by Fusion, at its option, in shares of Fusion’s common stock. The Purchase Price is subject to a working capital adjustment as well as a reduction for certain transaction expenses and any outstanding indebtedness of MegaPath as of the closing of the MegaPath Merger, in each case, as provided in the MegaPath Merger Agreement. At closing, \$2,500,000 of the Purchase Price will be deposited in an escrow account held by Citibank, N.A., as escrow agent, for one (1) year, to secure indemnification obligations in favor of Fusion under the MegaPath Merger Agreement.

A full description of each of the foregoing events is contained in our Current Report on Form 8-K which was filed with the Securities and Exchange Commission on May 10, 2018.

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

The following discussion should be read in conjunction with the information contained in our unaudited consolidated financial statements and the notes thereto appearing elsewhere herein and in conjunction with the Management’s Discussion and Analysis set forth in the Company’s 2017 Form 10-K.

Certain statements and the discussion contained herein regarding the Company’s business and operations may include “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements consist of any statement other than a recitation of historical fact and can be identified by the use of forward-looking terminology such as “may,” “plans,” “expect,” “anticipate,” “intend,” “estimate” or “continue” or the negative thereof or other variations thereof or comparable terminology. The reader is cautioned that all forward-looking statements are speculative, and there are certain risks and uncertainties that could cause actual events or results to differ from those referred to in such forward-looking statements. The primary risk of the Company is its ability to attract new capital to execute its comprehensive business strategy. There may be additional risks associated with the integration of businesses following an acquisition, the Company’s ability to comply with the terms of its credit facilities, competitors with broader product lines and greater resources, emergence into new markets, natural disasters, acts of war, terrorism or other events beyond the Company’s control and the other factors identified by the Company from time to time in its filings with the SEC. However, the risks included should not be assumed to be the only risks that could affect future performance. All forward-looking statements included are made as of the date hereof, based on information available to the Company as of the date thereof, and the Company assumes no obligation to update any forward-looking statements.

**OVERVIEW**

**Our Business**

We offer a comprehensive suite of cloud communications, cloud connectivity, cloud computing and managed cloud-based applications to small, medium and large businesses. Our advanced, proprietary cloud services platforms, as well as our state-of-the art switching systems, enable the integration of leading edge solutions in the cloud, increasing customer collaboration and productivity by seamlessly connecting employees, partners, customers and vendors.

We are focused on becoming our business customers’ single source for leveraging the increasing power of the cloud, providing a robust package of what we believe to be the essential services that form the foundation for their successful migration to, and efficient use of, the cloud. Our core Business Services products and services include cloud voice and Unified Communications as a Service, improving communication and collaboration on virtually any device, virtually anywhere, cloud connectivity services, securely and reliably connecting customers to the cloud with managed network solutions that are designed to increase quality and optimize network efficiency and contact center solutions. Our cloud computing and Infrastructure as a Service solutions are designed to provide our larger enterprise customers with a platform on which additional cloud services can be layered. Complemented by our Software as a Service solutions, such as security and business continuity, our advanced cloud offerings include private and hybrid cloud, storage, backup and recovery and secure file sharing that allow our customers to experience the increased efficiencies and agility delivered by the cloud. The Company’s cloud-based services are flexible, scalable and rapidly deployed, reducing our customers’ cost of ownership while increasing their productivity.

We continue to focus our sales and marketing efforts on developing vertically oriented solutions for targeted markets that require the kind of specialized solutions made possible by our state-of-the-art network and advanced services platforms. Our vertically oriented solutions, which are currently focused on healthcare, legal, hospitality and real estate, offer a substantial opportunity to gain additional market share. We intend to accelerate the growth of our business with the goal of increasing the portion of our total revenue derived from this higher margin.

**CRITICAL ACCOUNTING POLICIES AND ESTIMATES**

Our discussion and analysis of financial condition and results of operations are based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”). The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and the related disclosure of contingent liabilities. We base these estimates on our historical experience and on various other assumptions that we believe to be reasonable under the circumstances, and these estimates form the basis for our judgments concerning the carrying values of assets and liabilities that are not readily apparent from other sources. We periodically evaluate these estimates and judgments based on available information and experience. Actual results could differ from our estimates under different assumptions and conditions. If actual results significantly differ from our estimates, our financial condition and results of operations could be materially impacted.

We have identified the policies and significant estimation processes discussed below as critical to our operations and to an understanding of our results of operations. For a detailed discussion on the application of these and other accounting policies, see Note 2 to the Consolidated Financial Statements included in the 2017 Form 10-K.

### **Revenue Recognition**

We recognize revenue upon transfer of goods or services to a customer at an amount that reflects the expected consideration to be received in exchange for those goods or services. We use a five-step approach for recognizing revenue: (i) identification of the contract, (ii) identification of the performance obligations, (iii) determination of the transaction price, (iv) allocation of the transaction price to the performance obligations, and (v) recognition of revenue as the entity satisfies the performance obligations. These criteria for revenue recognition may require a company to use more judgment and make more estimates. We record provisions against revenue for billing adjustments, which are based upon estimates derived from factors that include, but are not limited to, historical results, analysis of credits issued and current economic trends. The provisions for revenue adjustments are recorded as a reduction of revenue at the time revenue is recognized.

As a result of the adoption of ASC 606 effective January 1, 2018, we now defer certain installation revenues and installation costs and recognize these revenues and costs ratably over 48-month period. The implementation impact of ASC 606 is not material to the Company's financial statements.

Our revenue includes monthly recurring charges ("MRC") to customers for whom services are contracted over a specified period of time, and variable usage fees charged to customers that purchase our business products and services. Revenue recognition commences after the provisioning, testing and acceptance of the service by the customer. MRC continues until the expiration of the contract, or until cancellation of the service by the customer. To the extent that payments received from a customer are related to a future period, the payment is recorded as deferred revenue until the service is provided or the usage occurs.

### **Cost of Revenues**

Our cost of revenues include the MRC associated with certain platform services purchased from other service providers, the MRC associated with private line services and the cost of broadband Internet access used to provide service to these business customers.

### **Fair Value of Financial Instruments**

The carrying value of certain financial instruments such as accounts receivable, accounts payable and accrued expenses, approximates their fair values due to their short term nature. Some of the warrants issued in conjunction with the issuance of our debt and equity securities are accounted for in accordance with the guidance contained in Accounting Standards Codification ("ASC") Topic 815, Derivatives and Hedging. For these warrant instruments that are not deemed to be indexed to Fusion's stock, we classify the warrant instrument as a liability at its fair value and adjust the instrument to fair value at each reporting period. This liability is subject to re-measurement at each balance sheet date until the underlying warrants are exercised or as they expire, and any change in fair value is recognized in our statement of operations. The fair values of these warrants have been estimated using option pricing and other valuation models, and the quoted market price of Fusion common stock.

### **Accounts Receivable**

Accounts receivable is recorded net of an allowance for doubtful accounts. On a periodic basis, we evaluate our accounts receivable and adjust the allowance for doubtful accounts based on our history of past write-offs and collections and current credit conditions. Specific customer accounts are written off as uncollectible if the probability of a future loss has been established, collection efforts have been exhausted and payment is not expected to be received.

### **Impairment of Long-Lived Assets**

We periodically review long-lived assets, including intangible assets, for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be fully recoverable. If an impairment indicator is present, we evaluate recoverability by a comparison of the carrying amount of the asset to future undiscounted net cash flows expected to be generated by the asset. If the carrying value of the asset exceeds the projected undiscounted cash flows, we are required to estimate the fair value of the asset and recognize an impairment charge to the extent that the carrying value of the asset exceeds its estimated fair value.

Impairment testing for goodwill is performed in the fourth fiscal quarter of each year. The impairment test for goodwill uses a two-step approach, which is performed at the reporting unit level. We have determined that our reporting units are our operating segments since that is the lowest level at which discrete, reliable financial and cash flow information is available. The authoritative guidance provides entities with an option to perform a qualitative assessment to determine whether a quantitative analysis is necessary. We recorded an impairment charge of \$1.2 million in the three months ended March 31, 2018. The Company did not record any impairment charges during the three months ended March 31, 2017.

### Income Taxes

We account for income taxes in accordance with U.S. GAAP, which requires the recognition of deferred tax liabilities and assets for the expected future income tax consequences of events that have been recognized in our financial statements. Deferred income tax assets and liabilities are computed for temporary differences between the financial statement and tax bases of assets and liabilities that will result in future taxable or deductible amounts, based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established to reduce deferred income tax assets when we determine that it is more likely than not that we will fail to generate sufficient taxable income to be able to utilize the deferred tax assets.

### Recently Issued Accounting Pronouncements

In July 2017, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2017-11, *Earnings Per Share (Topic 260), Distinguishing Liabilities from Equity (Topic 480), Derivatives and Hedging (Topic 815)*. The amendments in Part I of this update change the classification analysis of certain equity-linked financial instruments (or embedded features) with down round features. When determining whether certain financial instruments should be classified as liabilities or equity instruments, a down round feature no longer precludes equity classification when assessing whether the instrument is indexed to an entity’s own stock. The amendments also clarify existing disclosure requirements for equity-classified instruments. As a result, a freestanding equity-linked financial instrument (or embedded conversion option) no longer would be accounted for as a derivative liability at fair value as a result of the existence of a down round feature. This standard is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, with early adoption permitted. The Company is currently evaluating the effect that the new guidance will have on its financial statements and related disclosures.

In February 2016, the FASB issued ASU No. 2016-02, *Leases*, which is effective for fiscal years, and interim periods within those years, beginning after December 15, 2018 with early adoption permitted. Under ASU 2016-02, lessees will be required to recognize for all leases at the commencement date a lease liability, which is a lessee’s obligation to make lease payments arising from a lease measured on a discounted basis, and a right to-use asset, which is an asset that represents the lessee’s right to use or control the use of a specified asset for the lease term. The Company is currently evaluating the effect that the new guidance will have on its financial statements and related disclosures.

In May 2014, the FASB issued new guidance related to revenue recognition, ASU 2014-09, *Revenue from Contracts with Customers* (“ASC 606”), which outlines a comprehensive revenue recognition model and supersedes most current revenue recognition guidance. The new guidance requires a company to recognize revenue upon transfer of goods or services to a customer at an amount that reflects the expected consideration to be received in exchange for those goods or services. ASC 606 defines a five-step approach for recognizing revenue: (i) identification of the contract, (ii) identification of the performance obligations, (iii) determination of the transaction price, (iv) allocation of the transaction price to the performance obligations, and (v) recognition of revenue as the entity satisfies the performance obligations. The new criteria for revenue recognition may require a company to use more judgment and make more estimates than under the current guidance. The new guidance became effective in calendar year 2018. Two methods of adoption are permitted: (a) full retrospective adoption, meaning the standard is applied to all periods presented; or (b) modified retrospective adoption, meaning the cumulative effect of applying the new guidance is recognized at the date of initial application as an adjustment to the opening retained earnings balance.

In March 2016, April 2016 and December 2016, the FASB issued ASU No. 2016-08, *Revenue From Contracts with Customers (ASC 606): Principal Versus Agent Considerations*, ASU No. 2016-10, *Revenue From Contracts with Customers (ASC 606): Identifying Performance Obligations and Licensing*, and ASU No. 2016-20, *Technical Corrections and Improvements to Topic 606, Revenue From Contracts with Customers*, respectively, which further clarify the implementation guidance on principal versus agent considerations contained in ASU No. 2014-09. In May 2016, the FASB issued ASU 2016-12, *Revenue from Contracts with Customers, narrow-scope improvements and practical expedients* which provides clarification on assessing the collectability criterion, presentation of sales taxes, measurement date for non-cash consideration and completed contracts at transition. These standards became effective for the Company beginning with the first quarter of 2018.

## FUSION CONNECT, INC. AND SUBSIDIARIES

We adopted the new standard and related updates effective January 1, 2018, using the modified retrospective method of adoption. Adoption of this standard resulted in an adjustment to our accumulated deficit in the amount of \$0.1 million.

### RESULTS OF OPERATIONS

#### Three Months Ended March 31, 2018 Compared with Three Months Ended March 31, 2017

The following table summarizes the results of our consolidated operations for the three months ended March 31, 2018 and 2017:

	<u>2018</u>		<u>2017</u>	
	<u>\$</u>	<u>%</u>	<u>\$</u>	<u>%</u>
<b>Revenues</b>	\$ 29,038,043	100.0	\$ 28,481,039	100.0
Cost of revenues *	12,918,895	44.5	12,140,707	42.6
<b>Gross profit</b>	16,119,148	55.5	16,340,332	57.4
Depreciation and amortization	3,135,779	10.8	3,835,948	13.5
Selling, general and administrative expenses	13,947,995	48.0	13,613,661	47.8
Impairment charge	1,195,837	4.1	-	-
Total operating expenses	18,279,611	63.0	17,449,609	61.3
<b>Operating loss</b>	(2,160,463)	(7.4)	(1,109,277)	(3.9)
<b>Other (expenses) income:</b>				
Interest expense	(2,147,775)	(7.4)	(2,092,312)	(7.3)
Gain (loss) on change in fair value of derivative liability	194,312	0.7	(40,445)	(0.1)
Loss on disposal of property and equipment	(3,184)	(0.0)	(26,800)	(0.1)
Other income, net	89,558	0.3	116,520	0.4
Total other expenses	(1,867,089)	(6.4)	(2,043,037)	(7.2)
<b>Loss before income taxes</b>	(4,027,552)	(13.9)	(3,152,314)	(11.1)
Provision for income taxes	(14,050)	(0.0)	(7,811)	(0.0)
<b>Net loss from continuing operations</b>	\$ (4,041,602)	(13.9)	\$ (3,160,125)	(11.1)
<b>Net loss from discontinued operations</b>	(166,175)	(0.6)	(321,823)	(1.1)
<b>Net loss</b>	\$ (4,207,777)	(14.5)	\$ (3,481,948)	(12.2)

\*Exclusive of depreciation and amortization, shown separately.

#### Revenues

Consolidated revenues were \$29.0 million for the three months ended March 31, 2018, as compared to \$28.5 million for the three months ended March 31, 2017, an increase of \$0.5 million, or 2%. The increase is primarily attributable to revenue derived from the customer base acquired in March 2017. Only one month of revenue was included in Q1 2017 as opposed to three months in Q1 2018.

#### Cost of Revenues and Gross Profit

Cost of revenues was \$12.9 million for the three months ended March 31, 2018, as compared to \$12.1 million for the three months ended March 31, 2017.

Gross margin was 55.5% for the three months ended March 31, 2018, as compared to 57.4% for the three months ended March 31, 2017.

The increase in cost of revenue and decrease in gross margin was mainly due to higher circuit costs and lower margins from the customer base acquired in March 2017.

#### Depreciation and Amortization

Depreciation and amortization expense was \$3.1 million for the three months ended March 31, 2018, as compared to \$3.8 million for the same period of 2017. The decrease is primarily due to certain of our intangible assets becoming fully amortized and, to a lesser extent, some of our property and equipment becoming fully depreciated.

## FUSION CONNECT, INC. AND SUBSIDIARIES

### **Selling, General and Administrative Expenses**

Selling, general and administrative expenses (“SG&A”) for the three months ended March 31, 2018 was \$14.0 million, as compared to \$13.6 million for the three months ended March 31, 2017. This increase is driven primarily by higher sales commissions resulting from the customer base acquisition and an increase of \$0.2 million in transaction costs associated with an announced acquisition of Birch Communications Holdings, Inc., as these costs are expensed as incurred.

### **Impairment Charge**

During the three months ended March 31, 2018, we recorded an impairment charge on some of our property and equipment in the amount of \$1.2 million, with no comparable charge in the first three months of 2017.

### **Operating Loss**

Our operating loss of \$2.2 million for the three months ended March 31, 2018 represents an increase of approximately \$1.1 million from the operating loss for the three months ended March 31, 2017. The increase is mainly due to the 2018 impairment charge.

### **Other Expenses**

Other expenses, which includes interest expense, gains and losses on the change in fair value of the Company’s derivative liability, loss on the disposal of property and equipment and miscellaneous income and expense, was \$1.9 million for the three months ended March 31, 2018, as compared to \$2.0 million for the three months ended March 31, 2017. The decrease is mainly due to a gain on change in fair value of the derivative liability in 2018 of \$0.2 million, as compared to a loss of \$40,000 during the first quarter of 2017. Interest expense of \$2.1 million for the three months ended March 31, 2018 was largely unchanged from the same period a year ago.

### **Net Loss from continuing operations**

Our net loss from continuing operations for the three months ended March 31, 2018 was \$4.0 million, as compared to \$3.1 million for the three months ended March 31, 2017. The increase in net loss was mainly due to the increase in operating loss, partially offset by a decrease in other expenses.

## **LIQUIDITY AND CAPITAL RESOURCES**

Since our inception, we have incurred significant net losses. At March 31, 2018, we had working capital of \$13.2 million and stockholders’ equity of \$33.8 million. At December 31, 2017, we had a working capital deficit of \$15.4 million and a stockholders’ deficit of \$1.3 million. Our consolidated cash balance at March 31, 2018 was \$31.0 million. While our management projects that we have sufficient cash to fund our operations and meet our operating and debt obligations for the next twelve months, we may be required to either raise additional capital, limit our discretionary capital expenditures or borrow amounts available under our revolving credit facility to support our business plan. There is currently no commitment for additional funding of operations and there can be no assurances funds will be available on terms that are acceptable to us, or at all. See “Note 19 – Subsequent Events”.

In February 2018, we completed an underwritten public offering whereby Fusion issued 8,625,000 shares of its common stock and received net proceeds of \$38.2 million. The proceeds from this offering are being used to pay down certain indebtedness and for general corporate purposes.

We have never paid cash dividends on our common stock, and we do not anticipate paying cash dividends on our common stock in the foreseeable future. We intend to retain all of our earnings, if any, for general corporate purposes, and, if appropriate, to finance the further expansion of our business. Subject to the rights of holders of our outstanding preferred stock, any future determination to pay dividends is at the discretion of Fusion’s Board, and will be dependent upon our financial condition, operating results, capital requirements, general business conditions, the terms of our then existing credit facilities, limitations under Delaware law and other factors that Fusion’s Board and senior management consider appropriate.

The holders of our Series B-2 Preferred Stock are entitled to receive quarterly dividends at an annual rate of 6%. These dividends can be paid, at the Company’s option, either in cash or, under certain circumstances, in shares of Fusion common stock. For the three months ended March 31, 2018 we declared dividends of \$144,000 on the Series B-2 Preferred Stock, which, as permitted by the terms of such Series, was paid in the form of 3,985 shares of Fusion common stock.

## FUSION CONNECT, INC. AND SUBSIDIARIES

For the past several years we have relied primarily on the sale of Fusion's equity securities and the cash generated from our Business Services segment to fund our operations, and we issued additional debt to fund our acquisitions and growth strategy. On November 14, 2016, contemporaneously with an acquisition, we entered into a credit agreement (the "East West Credit Agreement") with East West Bank, as administrative agent and the lenders identified therein (collectively the "East West Lenders"). Under the East West Credit Agreement, the East West Lenders extended us a (i) \$65.0 million term loan and (ii) \$5.0 million revolving credit facility (which includes up to \$4 million in "swingline" loans that may be accessed on a short-term basis). The proceeds of the term loan were used to retire the \$40 million that was outstanding under a previously existing credit facility, and to fund the cash portion of the purchase price of the Aptix acquisition in the amount of \$23.1 million. See "Note 19 – Subsequent Events".

Borrowings under the East West Credit Agreement are evidenced by notes bearing interest at rates to be computed based upon either the then current "prime" rate of interest or "LIBOR" rate of interest, as selected by us at the time of borrowing. Interest on borrowings that we designate as "base rate" loans bear interest at the greater of the prime rate published by the Wall Street Journal or 3.25% per annum, in each case plus 2% per annum. Interest on borrowings that we designate as "LIBOR rate" loans bear interest at the LIBOR rate published by the Wall Street Journal, plus 5% per annum. The current interest rate is 6.75% per annum.

We are required to repay the term loan in equal monthly payments of \$541,667 until the maturity date of the term loan on November 12, 2021, when the remaining \$36.8 million of principal is due. Borrowings under the revolving credit facility are also payable on the November 12, 2021 maturity date of the facility. During the three months ended March 31, 2018, we paid down the \$1.5 million that was outstanding on the revolving credit facility as of December 31, 2017, and at March 31, 2018, \$55.1 million was outstanding under the term loan and no amounts were outstanding under the revolving credit facility.

Under the East West Credit Agreement:

- We are subject to a number of affirmative and negative covenants, including but not limited to, restrictions on paying indebtedness subordinate to our obligations to the East West Lenders, incurring additional indebtedness, making capital
- We are required to comply with various financial covenants, including leverage ratio, fixed charge coverage ratio and minimum levels of earnings before interest, taxes, depreciation and amortization; and our failure to comply with any of the restrictive or financial covenants could result in an event of default and accelerated demand for repayment of this indebtedness.
- We granted the East West Lenders security interests in all of our assets, as well as our 60% membership interest in FGS and the capital stock of our Fusion NBS Acquisition Corp. subsidiary ("FNAC") and each of its subsidiaries.
- Fusion and its subsidiaries other than FNAC and FGS (and future subsidiaries of both) guaranteed FNAC's obligations, including FNAC's repayment obligations thereunder.

On November 14, 2016, FNAC, Fusion and Fusion's subsidiaries other than FNAC entered into the Fifth Amended and Restated Securities Purchase Agreement (the "Praesidian Facility") with Praesidian Capital Opportunity Fund III, L.P., Praesidian Capital Opportunity Fund III-A, LP and United Insurance Company of America (collectively, the "Praesidian Lenders"). The Praesidian Facility amends and restates a prior facility, pursuant to which FNAC previously sold its Series A, Series B, Series C, Series D, Series E and Series F senior notes in an aggregate principal amount of \$33.6 million (the "SPA Notes"). The proceeds from the SPA Notes were used to finance previous acquisitions within our Business Services segment. These notes require payments of monthly interest in the amount of \$0.3 million and the entire principal amount of the notes are due May 12, 2022. The current interest rate is 10.8% per annum. See "Note 19 – Subsequent Events".

The Praesidian Facility contains financial covenants that are substantially similar to those contained in the East West Credit Agreement. At March 31, 2018, we were in compliance with all of the financial covenants under the East West Credit Agreement and the Praesidian Facility. Under the terms of the Merger with Birch, all amounts outstanding under the Praesidian Facility and the East West Credit Agreement, as well as substantially all of Birch's outstanding indebtedness, were refinanced with a larger senior credit facility at the time of closing.

The Company underwent a compliance audit for the use of certain software licenses by one of the Company's recently acquired businesses. The Company is negotiating with the software vendor with regard to a settlement and based upon correspondence and conversations with the vendor, the Company has recorded an accrual in accounts payable and accrued expenses in the accompanying consolidated balance sheet. There can be no assurances that this matter will be settled and, if settled, the amount that we would pay in any such settlement.

**FUSION CONNECT, INC. AND SUBSIDIARIES**

The following table sets forth a summary of our cash flows for the periods indicated:

	<b>Three Months ended March 31,</b>	
	<b>2018</b>	<b>2017</b>
Net cash (used in) provided by operating activities	\$ (6,291)	\$ 1,369,244
Net cash used in investing activities	(945,344)	(1,502,291)
Net cash provided by (used in) financing activities	29,586,144	(446,710)
Net increase (decrease) in cash and cash equivalents	28,634,509	(579,757)
Cash and cash equivalents, including restricted cash, beginning of period	2,557,541	7,249,063
Cash and cash equivalents, including restricted cash, end of period	31,192,050	6,669,306
Less cash and cash equivalents, discontinued operations, end of period	165,165	15,038
Cash and cash equivalents, including restricted cash of continued operations, end of period	<u>\$ 31,026,885</u>	<u>\$ 6,654,268</u>

Cash used in operating activities was \$6,000 for the three months ended March 31, 2018, as compared to cash provided by operating activities of \$1.4 million during the three months ended March 31, 2017.

The following table illustrates the primary components of our cash flows from operations:

	<b>Three Months ended March 31,</b>	
	<b>2018</b>	<b>2017</b>
Net loss from continuing operations	\$ (4,041,602)	\$ (3,160,125)
Net loss from discontinued operations	(166,175)	(321,823)
Net loss	(4,207,777)	(3,481,948)
Non-cash expenses, gains and losses	4,701,705	4,501,918
Changes in accounts receivable	1,459,401	179,518
Changes in accounts payable and accrued expenses	(1,949,917)	690,812
Other	(283,490)	(865,106)
Cash (used in) provided by operating activities - continuing operations	(113,903)	1,347,017
Cash provided by operating activities - discontinued operations	107,612	22,227
Net cash (used in) provided by operating activities	<u>\$ (6,291)</u>	<u>\$ 1,369,244</u>

Cash used in investing activities for the three months ended March 31, 2018 consists primarily of capital expenditures in the amount of \$1.0 million. Cash used in investing activities for the three months ended March 31, 2017 consists primarily of capital expenditures in the amount of \$1.0 million and payments related to acquisitions of approximately \$0.6 million.

Cash provided by financing activities was \$29.6 million for the three months ended March 31, 2018. During the first three months of 2018, we received net proceeds from a public offering of Fusion common stock in the amount \$38.2 million, made principal payments on the term loan and revolving credit facility under the East-West Credit Agreement of \$6.6 million and \$1.5 million, respectively, and made payments on capital lease obligations in the amount of \$0.3 million.

Cash used in financing activities for the three months ended March 31, 2017 was \$0.4 million, as we received proceeds from the exercise of common stock purchase warrants in the amount of \$0.8 million, made principal payments on the East West Credit Agreement term loan in the amount of \$0.8 million, made payments under capital lease obligations of \$0.2 million and paid down obligations under asset purchase agreements in the amount of \$0.2 million.

**Other Matters**

**Inflation**

We do not believe inflation has a significant effect on our operations at this time.

**Off Balance Sheet Arrangements**

At March 31, 2018, we have no off-balance sheet arrangements that have, or are reasonably likely to have, a current or future material effect on our financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

Disclosure under this section is not required for a smaller reporting company.

**Item 4. Controls and Procedures.**

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), that are designed to ensure that information required to be disclosed in Exchange Act reports is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures as of March 31, 2018. Based upon that evaluation and subject to the foregoing, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective to accomplish their objectives.

Our Chief Executive Officer and Chief Financial Officer do not expect that our disclosure controls or our internal controls will prevent all error and all fraud. The design of a control system must reflect the fact that there are resource constraints and the benefit of controls must be considered relative to their cost. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that we have detected all of our control issues and all instances of fraud, if any. The design of any system of controls also is based partly on certain assumptions about the likelihood of future events and there can be no assurance that any design will succeed in achieving our stated goals under all potential future conditions.

Effective January 1, 2018, we adopted the new revenue guidance under ASC Topic 606, *Revenue from Contracts with Customers*. The adoption of this guidance requires from the Company the implementation of new accounting processes and policies, including changes to our information systems, which changed the Company’s internal controls over financial reporting for revenue recognition and related disclosures. Other than the change noted above, there have been no other changes in our internal control over financial reporting that occurred during the three months ended March 31, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

**Item 1. Legal Proceedings.**

None.

**Item 1A. Risk Factors.**

Risk factors describing the major risks to our business can be found under Item 1A, “Risk Factors,” in our 2017 Form 10-K. There have been no material changes to our risk factors from those previously disclosed in the 2017 Form 10-K.

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

See the disclosure set forth in “Note 19 – Subsequent Events” under the captions “Completion of the Acquisition of Birch Communications”, “Private Placement of Common Stock” and “Private Placement of Series D Preferred Stock”, which information is incorporated herein by this reference.

**Item 3. Defaults Upon Senior Securities.**

None.

**Item 4. Mine Safety Disclosures.**

Not applicable.

**Item 5. Other Information.**

None.

**Item 6. Exhibits**

EXHIBIT NO.	DESCRIPTION
<a href="#">10.1</a>	Employment Agreement, dated as of February 6, 2017, by and between Birch Communications, LLC (formerly Birch Communications, Inc.) and Kevin M. Dotts.
<a href="#">31.1</a>	Certification of the Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
<a href="#">31.2</a>	Certification of the Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
<a href="#">32.1</a>	Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
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101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
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101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

**FUSION CONNECT, INC. AND SUBSIDIARIES**

**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.

**FUSION CONNECT, INC.**

May 15, 2018

By: /s/ Kevin M. Dotts

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Kevin M. Dotts  
Executive Vice President, Chief Financial  
Officer and Principal Accounting Officer

## FUSION CONNECT, INC. AND SUBSIDIARIES

### Index to Exhibits

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**Certification of the Chief Executive Officer**

I, **Matthew D. Rosen**, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the quarter ended March 31, 2018 (the "Report") of Fusion Connect, Inc., a Delaware corporation ("the Registrant");
2. Based on my knowledge, this Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Report;
3. Based on my knowledge, the financial statements, and other financial information included in this Report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this Report;
4. The Registrant's other certifying officer and I, are responsible for establishing and maintaining disclosure controls and procedures as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) and internal control over financial reporting as defined in Exchange Act Rules 13a-15(f) and 15(d)-15(f) for the Registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this Report based on such evaluation; and
  - (d) Disclosed in this Report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and
5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's Board of Directors;
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

**FUSION CONNECT, INC.**

May 15, 2018

By: /s/ **MATTHEW D. ROSEN**

Matthew D. Rosen

Chief Executive Officer

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**Certification of the Chief Financial Officer**

I, **Kevin M. Dotts**, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the quarter ended March 31, 2018 (the "Report") of Fusion Connect, Inc., a Delaware corporation ("the Registrant");
2. Based on my knowledge, this Report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this Report;
3. Based on my knowledge, the financial statements, and other financial information included in this Report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this Report;
4. The Registrant's other certifying officer and I, are responsible for establishing and maintaining disclosure controls and procedures as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) and internal control over financial reporting as defined in Exchange Act Rules 13a-15(f) and 15(d)-15(f) for the Registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the Registrant's disclosure controls and procedures and presented in this Report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this Report based on such evaluation; and
  - (d) Disclosed in this Report any change in the Registrant's internal control over financial reporting that occurred during the Registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Registrant's internal control over financial reporting; and
5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the Registrant's auditors and the audit committee of the Registrant's Board of Directors;
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the Registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal control over financial reporting.

**FUSION CONNECT, INC.**

May 15, 2018

By: /s/ KEVIN M. DOTTS

Kevin M. Dotts

Executive Vice President, Chief Financial Officer and Principal Accounting Officer

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**CERTIFICATION PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002 (SUBSECTIONS (A) AND (B) OF SECTION 1350, CHAPTER 63 OF TITLE 18, UNITED STATES CODE)**

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), the undersigned officer of Fusion Connect, Inc., a Delaware corporation (the "Company"), does hereby certify that:

The Quarterly Report on Form 10-Q for the quarter ended March 31, 2018 (the "Form 10-Q") of the Company fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

**FUSION CONNECT, INC.**

May 15, 2018      By: /s/ MATTHEW D. ROSEN  
Matthew D. Rosen  
Chief Executive Officer

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement has been provided to the Company and will be retained by the Company and furnished to the SEC or its staff upon request.

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**CERTIFICATION PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002 (SUBSECTIONS (A) AND (B) OF SECTION 1350, CHAPTER 63 OF TITLE 18, UNITED STATES CODE)**

Pursuant to section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of section 1350, chapter 63 of title 18, United States Code), the undersigned officer of Fusion Connect, Inc., a Delaware corporation (the "Company"), does hereby certify that:

The Quarterly Report on Form 10-Q for the quarter ended March 31, 2018 (the "Form 10-Q") of the Company fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of the Company.

**FUSION CONNECT, INC.**

May 15, 2018

By: /s/ KEVIN M. DOTTS

Kevin M. Dotts

Executive Vice President, Chief Financial Officer and Principal Accounting Officer

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement has been provided to the Company and will be retained by the Company and furnished to the SEC or its staff upon request.

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## EXECUTIVE EMPLOYMENT AGREEMENT

**THIS EXECUTIVE EMPLOYMENT AGREEMENT** (this "Agreement") is made effective as of the 6<sup>th</sup> day of February, 2017 (the "Effective Date"), by and between BIRCH COMMUNICATIONS, INC., a Georgia corporation ("Company"), and **Kevin M. Dotts**, a resident of the State of Georgia (referred to herein as "You", "Your", or "Yours").

## RECITALS

**WHEREAS**, the Company and its Affiliates (defined below) provide communications, network, cloud, and IT solutions to small, mid-sized, enterprise, and wholesale businesses in the United States and Canada, offering enterprise-class cloud hosted phone systems; data center environments with virtual and physical solutions; and file storage solutions for confidential data; and providing voice services, including basic phone line, VoIP, hosted PBX, and mobile services; network Internet services, such as broadband, Internet, and multi-protocol label switching (MPLS) services; and information technology services, including remote monitoring, software management, helpdesk, voice migration, and cloud migration services; and also providing facilities-based wholesale telecommunications services to competitive local exchange carriers, Internet service providers, VoIP providers, and resellers (the "Business");

**WHEREAS**, the Company has determined that, in view of Your professional knowledge, expertise and experience, Your services as an executive of the Company will be of great value to the Company and its Affiliates and, accordingly, the Company desires to enter into this Agreement with You as set forth herein in order to secure such services as determined by the Company; and

**WHEREAS**, You desire to serve as an executive of the Company on the terms and conditions set forth herein.

**NOW, THEREFORE**, for and in consideration of Your employment by the Company, the above premises and the mutual agreements hereinafter set forth, You and the Company agree as follows:

**1. Definitions.**

(a) "Affiliate" means any corporation, limited liability company, partnership, association, joint venture or similar business entity of which (i) if a corporation, a majority of the total voting power of shares of stock entitled (without regard to the occurrence of any contingency) to vote in the election of directors, managers, or trustees thereof is at the time owned or controlled, directly or indirectly, by the Company or one or more of the other Subsidiaries of the Company or a combination thereof, or (ii) if a limited liability company, partnership, association, or other business entity (other than a corporation), a majority of partnership or other similar ownership interest thereof is at the time owned or controlled, directly or indirectly, by the Company or one or more Subsidiaries of the Company or a combination thereof or such the Company is the general partner or managing member of such a partnership or limited liability company, respectively. Unless the context suggests otherwise, all references to "Affiliate" in this Agreement will refer to a direct or indirect subsidiary of the Company.

(b) "Cause" means (i) Your commission of any act of fraud or dishonesty with respect to the Company, or any of its Affiliates, or any of their customers or suppliers that is materially harmful to the Company, including to its reputation; (ii) Your conviction of any felony; (iii) Your reporting to work under the influence of alcohol or illegal drugs, the use of illegal drugs (whether or not at the workplace) or other repeated conduct which causes the Company or any of its Affiliates substantial public disgrace or disrepute or substantial economic harm; (iv) Your commission of one or more acts of gross negligence or willful misconduct, after written notice to You specifying such acts and a reasonable opportunity during a period of no fewer than thirty (30) days to cure such acts; or (v) Your material breach of Sections 5, 6, 7, 8 or 9 of this Agreement, after written notice to You specifying such acts and a reasonable opportunity during a period of no fewer than thirty (30) days to cure such acts.

(c) "Change in Circumstance" means (i) a substantial adverse alteration in the nature or status of Your responsibilities without Your written consent, (ii) without Your written consent, a reduction in Base Salary other than a reduction of up to five percent (5%) generally applicable to all similarly situated executives of the Company, (iii) without Your written consent, relocation of the Company's principal place of business outside a fifty (50) mile radius of Atlanta, Georgia or (iv) a material breach by the Company or Holdings of a material provision of this Agreement; in the case of each of clauses (i) through (iv), after written notice by You to the Company specifying such acts within sixty (60) days following the occurrence thereof and a reasonable opportunity during a period of no fewer than thirty (30) days to cure such acts.

(d) "Change in Control" means (i) the transfer of all or substantially all of the Company's total assets on a consolidated basis to an unaffiliated third party; or (ii) any sale, transfer, or issuance or series of sales, transfers and/or issuances of voting securities of the Company or its sole shareholder, Birch Communications Holdings, Inc. ("Holdings") which results in any Person or group of Persons (as the term "group" is used under the Securities Exchange Act of 1934), other than Holcombe T. Green, Jr., and R. Kirby Godsey, and their respective spouses and children (and trusts therefor), and affiliates controlled by any of them, owning, directly or indirectly, more than 50% of such voting securities outstanding at the time of such sale, transfer or issuance or series of sales, transfers and/or issuances. Notwithstanding the foregoing, as to any compensation that is subject to Code Section 409A (defined below), in no event shall a Change in Control be deemed to occur, for purposes of this Agreement, if it does not constitute a qualifying Change in Control event under Code Section 409A.

(e) "Code" means the Internal Revenue Code of 1986, as amended, or any successor thereto.

(f) "Person" means an individual, a partnership, a corporation, a limited liability company, an association, a joint stock company, a trust, a joint venture, an unincorporated organization and a governmental entity or any department, agency or political subdivision thereof.

(g) "Total Disability" means Your inability, through physical or mental illness or accident, to perform the essential functions of Your usual duties and responsibilities hereunder (as such duties are constituted on the date of the commencement of such disability) for a period of at least ninety (90) consecutive days following reasonable accommodation, all as determined by an independent medical doctor licensed to practice medicine in the State of Georgia retained by the Board to make such determination. Total Disability shall be deemed to have occurred on the first day following the expiration of such period.

## **2. Employment; Duties.**

(a) During the Employment Period, You shall serve as the Chief Financial Officer of the Company and shall have the normal duties, responsibilities, functions and authority of a Chief Financial Officer, subject to the power and authority of the Chief Executive Officer and the Board of Directors (the "Board") of the Company and Holdings. During the Employment Period, You shall render such administrative, financial and other executive and managerial services to the Company and its Affiliates which are consistent with Your position as a Chief Financial Officer.

(b) During the Employment Period, You shall report to the Chief Executive Officer and Board of Directors, and shall devote Your best efforts and Your full business time and attention (except for permitted vacation periods and reasonable periods of illness or other incapacity) to the business and affairs of the Company and its Affiliates; You shall perform Your duties, responsibilities and functions to the Company and its Affiliates hereunder to the best of Your abilities in a diligent, trustworthy, professional and efficient manner and shall comply with the Company's and its Affiliates' policies and procedures in all material respects. In performing Your duties and exercising Your authority under this Agreement, You shall support and implement the business and strategic plans approved from time to time by the Board. So long as You are employed by the Company or any of its Affiliates, You shall not, without the prior written consent of the Board, accept other employment or perform other services for compensation other than for the Board and its Affiliates.

## **3. Compensation.**

(a) (1) You shall be paid a base salary of \$375,000 per year. The Board shall review Your base salary annually during the Employment Period and, in its sole discretion, may alter such base salary from time to time in accordance with the terms of this Agreement after notice to You. The annual base salary payable to You under this Section 3(a), as the same may be adjusted from time to time, shall hereinafter be referred to as the "Base Salary". The Base Salary shall accrue and be due and payable in equal, or as nearly equal as practicable, bi-weekly installments and the Company may deduct from each such installment all amounts required to be deducted and withheld in accordance with applicable federal and state income, FICA and other withholding tax requirements.

(2) If the Employment Period shall begin on other than the first business day of a pay period and/or if the Employment Period shall terminate on other than the last day of a pay period, Your compensation for such pay period shall be prorated according to the number of days during such pay period within the Employment Period.

(3) As of the end of each calendar year during the Employment Period, You shall be eligible to receive a cash bonus as determined by the Board in its sole discretion of up to an amount equal to, at target levels of performance, 75% of Base Salary paid during such calendar year (the "Bonus Payments", and the Bonus Payment at target levels of performance, the "Target Bonus"). The Bonus Payment shall be based on EBITDA, cash flow, revenue and/or other financial goals mutually agreed by the Board and the CEO. All payments under this Section 3(a)(3) shall be subject to all withholdings in accordance with applicable federal and state income, FICA and other withholding tax requirements and shall be paid in accordance with the Company's practice for the timing of making bonus payments to its employees, but in any event on or prior to March 15 of the year following the year in which the Bonus Payment relates.

(4) The Company shall reimburse You up to \$5,000 for Your attorney's fees incurred in reaching this Agreement.

**(5) You will also be eligible to receive the Equity Appreciation Bonus set forth on Exhibit C attached hereto, in accordance with its terms and conditions, which Holdings agrees to pay. The Company has no obligation in respect of the Equity Appreciation Bonus.**

(a) While You are performing the services described herein, the Company shall, upon Your request, reimburse You for all reasonable and necessary expenses incurred by You in connection with the performance of Your duties of employment hereunder. All reimbursements to You for expenses shall be reasonably documented and timely submitted for reimbursement to the Company in accordance with the Company's normal reimbursement policies. Such reimbursements shall be made as soon as administratively practical following an appropriate request, provided You submit Your request within thirty (30) days after You incur such expenses. Notwithstanding anything to the contrary herein, in the event of a termination of this Agreement for any reason, including for Cause, You shall be entitled to any reimbursements accrued through Your termination date in accordance with this paragraph.

(b) During the Employment Period, You shall be eligible to participate in all health, medical, disability and group term life insurance, and other employee welfare benefit plans and fringe benefits of the Company (and, to the extent applicable, Your eligible family members and dependents) in accordance with any group plan or program established by the Company and the terms and conditions thereof. You shall also be eligible to participate in any qualified and non-qualified retirement savings, defined benefit, and deferred compensation plans that the Company sponsors for similarly situated executives.

(c) You shall receive four (4) weeks paid time off during each full twelve (12) month period of the Employment Period.

#### **4. Term; Termination.**

(a) The term of Your employment under this Agreement shall commence on the Effective Date and shall end on February 6, 2020; provided that unless terminated pursuant to the terms and conditions of this Agreement, this Agreement and Your employment hereunder shall be automatically renewed on the terms and conditions set forth herein for additional twelve (12) month periods (the "Employment Period"). Notwithstanding the foregoing, (i) the Employment Period shall terminate immediately upon Your resignation (with or without a Change in Circumstance), death or Total Disability, and (ii) the Employment Period may be terminated by the Company at any time for Cause or without Cause. Except as otherwise provided herein, any termination of the Employment Period shall be effective as specified in a written notice from the Company to You. Solely for purposes of determining Your right to compensation under Section 4(b) below (to the extent such compensation is subject to Code Section 409A), You will not be considered to have terminated Your employment, and the Employment Period will not be deemed to have terminated, unless You have a "separation from service" within the meaning of Code Section 409A (as defined below).

(b) If (x) the Employment Period is terminated by the Company without Cause (excluding, for clarity, a termination by reason of Your death or Total Disability) or by You as a result of a Change in Circumstance or (y) prior to the end of the Employment Period, the Company does not offer in writing to continue Your employment following the end of the Employment Period upon substantially the same terms as provided in this Agreement (or as otherwise mutually agreed between You and the Company), and You elect to resign from the Company effective as of the end of the Employment Period, You shall be entitled to receive Your Base Salary earned through the date of termination or resignation, plus any accrued but unpaid Bonus Payments and payment for any unused vacation time, and You shall be entitled to any other salary, compensation or benefits from the Company or its Affiliates as otherwise specifically earned and/or vested as provided for under the Company's employee benefit plans, and the Company shall pay You for any reimbursable expenses owed to You through the effective date of the termination or Your employment. In addition:

(1) You shall be paid severance pay equal to the sum of twelve (12) months of Base Salary, such severance pay to be paid via payroll continuation over the period of twelve (12) months following the effective date of the termination of Your employment (the "Severance Period"), with the payments being made on a bi-weekly basis and commencing as provided in Section 4(b)(3), and you shall be entitled to payment or reimbursement of all premiums for medical benefits elected by You pursuant to the continuation of medical coverage under Section 4980B of the Code during the Severance Period (collectively, the "Severance Payments"); and

(2) You shall be entitled to the foregoing Severance Payments if and only if (i) You have executed and delivered to the Company a General Release similar in form and substance as set forth in Exhibit A attached hereto and (ii) the General Release has become effective, in each case within 60 days of Your termination of employment, and only for so long as You have not revoked or breached the provisions of the General Release or materially breached the provisions of Sections 5, 6, 7, 8 or 9 hereof. You shall not be entitled any other salary, compensation or benefits after termination of the Employment Period, except as otherwise specifically provided for in the Company's employee benefit plans and in this Agreement.

(3) To the extent that Severance Payments or benefits pursuant to this Agreement are conditioned upon the execution and delivery by You of a release of claims, You shall forfeit all rights to such payments and benefits unless such release is signed and delivered (and no longer subject to revocation, if applicable) within sixty (60) days following the date of Your termination of employment. If the foregoing release is executed and delivered and no longer subject to revocation as provided in the preceding sentence, then the following shall apply:

(i) To the extent any such cash payment or continuing benefit to be provided is not "deferred compensation" for purposes of Code Section 409A, then such payment or benefit shall commence upon the first scheduled payment date immediately after the date the General Release is executed and no longer subject to revocation (the "Release Effective Date"). The first such cash payment shall include payment of all amounts that otherwise would have been due prior to the Release Effective Date under the terms of this Agreement applied as though such payments commenced immediately upon Your termination of employment, and any payments made thereafter shall continue as provided herein. The delayed benefits shall in any event expire at the time such benefits would have expired had such benefits commenced immediately following Your termination of employment.

(ii) To the extent any such cash payment or continuing benefit to be provided is “deferred compensation” for purposes of Code Section 409A, then such payments or benefits shall be made or commence upon the sixtieth (60) day following Your termination of employment. The first such cash payment shall include payment of all amounts that otherwise would have been due prior thereto under the terms of this Agreement had such payments commenced immediately upon Your termination of employment, and any payments made thereafter shall continue as provided herein. The delayed benefits shall in any event expire at the time such benefits would have expired had such benefits commenced immediately following Your termination of employment.

(b) In the event that (i) Your employment is terminated by the Company for Cause, (ii) You resign without a Change in Circumstance or (iii) Your employment is terminated by reason of Your death or Total Disability, You shall only be entitled to receive Your Base Salary earned through the date of termination or resignation and any accrued but unpaid Bonus Payments as of the date of termination and payment for any unused vacation time, and You shall not be entitled to any other salary, compensation or benefits from the Company or its Affiliates thereafter, except as otherwise specifically earned and/or vested as provided for under the Company’s employee benefit plans, and the Company shall pay You for any reimbursable expenses owed to You through the effective date of the termination or Your employment.

(c) The effective date of the termination of Your employment with the Company is referred to hereinbelow as the “Employment Termination Date”.

## **5. Confidential Information.**

(a) Obligation to Maintain Confidentiality. You acknowledge that the continued success of the Company and its Affiliates depends upon the use and protection of a large body of confidential and proprietary information. All of such confidential and proprietary information now existing or to be developed in the future will be referred to in this Agreement as “Confidential Information.” Confidential Information shall be deemed to consist of all information of any sort (whether obtained prior to or after the date hereof) that is (i) related to the Company’s or its Affiliates’ (or their respective predecessors as it relates to the Business) current or potential business and (ii) is not generally or publicly known. Confidential Information includes, without specific limitation, the information, observations and data obtained by You during the course of Your employment with the Company concerning the business and affairs of the Company and its Affiliates (and during the course of Your employment with the Company’s and its Affiliates’ predecessors concerning the Business), information concerning acquisition opportunities in or reasonably related to the Company’s or its Affiliates’ business or industry of which You become aware during the Employment Period, the persons or entities that are current, former or prospective suppliers or customers of any one or more of them during Your employment with the Company, as well as development, transition and transformation plans, methodologies and methods of doing business, strategic, marketing and expansion plans, including plans regarding planned and potential customers, financial and business plans, employee lists and telephone numbers, new and existing programs and services, prices and terms, customer service, integration processes, requirements and costs of providing service, support and equipment. Therefore, You agree that You shall not disclose to any unauthorized person or use for Your own account any of such Confidential Information without the Board’s prior written consent, unless and to the extent that any Confidential Information (i) is or subsequently becomes generally known to and available for use by the public other than as a result of Your acts; (ii) is rightfully received by You from a third party who, to Your knowledge, is not under a duty of confidentiality; or (iii) is required to be disclosed pursuant to any applicable law or court order. You agree to deliver to the Company at the end of the Employment Period, or at any other time the Company may request in writing, all memoranda, notes, plans, records, reports and other documents (and copies thereof) relating to the business of the Company or its Affiliates (including, without limitation, all Confidential Information) that You may then possess or have under Your control.

(b) Third Party Information. You understand that the Company and its Affiliates will receive from third parties confidential or proprietary information ("Third Party Information") subject to a duty on the Company's and its Affiliates' part to maintain the confidentiality of such information and to use it only for certain limited purposes. During the Employment Period and thereafter, and without in any way limiting the provisions of Section 5(a) above, You will hold Third Party Information in the strictest confidence and will not disclose to anyone (other than personnel of the Company or its Affiliates who need to know such information in connection with their work for the Company or such Affiliates) or use, except in connection with Your work for the Company or its Affiliates, Third Party Information unless expressly authorized by a member of the Board in writing.

## **6. Intellectual Property, Inventions and Patents.**

(a) You acknowledge that all discoveries, concepts, ideas, inventions, innovations, improvements, developments, methods, methods of doing business, processes, programs, designs, analyses, drawings, reports, data, software, trade secrets, firmware, logos, software, patent applications, copyrightable work and mask work (whether or not including any confidential information) and all registrations or applications related thereto, all other proprietary information and all similar or related information (whether or not patentable) which relate to the Company's or any of its Affiliates' actual or anticipated business, research and development or existing or future products or services and which are conceived, developed, acquired, contributed to, made, or reduced to practice by You (whether alone or jointly with others) while employed by the Company or its predecessor and their Affiliates, whether before or after the date of this Agreement (collectively, "Work Product"), belong to the Company or such Affiliate. The provisions of this Section 6 will apply to Work Product which is first reduced to practice and developed during the Employment Period, whether or not further development or reduction to practice may take place after termination of this Agreement.

(b) You shall promptly disclose Work Product to the Board and, at the Company's expense, perform all actions reasonably requested by the Board (whether during or after the Employment Period) to establish and confirm such ownership (including, without limitation, providing testimony and executing assignments, consents, powers of attorney and other instruments).

(c) Any copyrightable work falling within the definition of Work Product shall be deemed a "work made for hire" under the copyright laws of the United States, and ownership of all rights therein shall vest in the Company or its Affiliate. To the extent that any Work Product is not deemed to be a "work made for hire," You hereby assign and agree to assign to the Company or such Affiliate all right, title and interest, including without limitation, the intellectual property rights that You may have in and to such Work Product. You agree to execute any documents and take any actions (at the Company's expense) that may be legally required to effect and confirm such transfer and assignment and waiver.

(d) You understand, however, that there is no obligation being imposed on You to assign to the Company or any Affiliate, any invention falling within the definition of Work Product for which no equipment, supplies, facility, or trade secret information of the Company or any of its Affiliates (or any of their predecessors) was used and that was developed entirely on Your own time, unless: (i) such Work Product relates to the Company's, or its Affiliates' businesses or their actual or demonstrably anticipated research or development, or (ii) the Work Product results from any work performed by You for the Company, or its Affiliates under this Agreement.

(e) You have identified and listed on Exhibit B all Work Product that is or was owned by You or was written, discovered, made, conceived or first reduced to practice by You alone or jointly with another person prior to Your employment under this Agreement and with the Company's and its Affiliates' predecessors. If no such Work Product is listed, You represent to the Company that You do not now nor have You ever owned, nor have You made, any such Work Product.

**7. Non-Competition.** In further consideration of the compensation to be paid to You hereunder, You acknowledge that during the course of Your employment with the Company and its Affiliates You will become familiar with the Company's and its Affiliates' trade secrets and with other Confidential Information concerning the Company and its Affiliates and that Your services shall be of special, unique and extraordinary value to the Company and its Affiliates, and therefore, in further consideration of the compensation to be paid to You hereunder, You agree that during Your employment with the Company or any of its Affiliates and for a period of twelve (12) months after termination of Your employment with the Company and its Affiliates for any reason, You shall not, directly or indirectly, within the Territory (as defined below), provide Services (as defined below) to or for the benefit of any Person (including You) which is at the time engaged in the Business. As used herein, the "Territory" shall mean the United States and "Services" shall mean services provided by You to the Company or any of its Affiliates during the one year period immediately preceding the termination of Your employment with the Company.

**8. Customer Non-Solicitation.** You agree that during Your employment with the Company and for a period of twelve (12) months after termination of Your employment with the Company for any reason, You will not directly or indirectly on Your own behalf or on behalf of any other Person, except on behalf of the Company, (i) solicit or call upon any customer or client or Prospective Customer (as defined below) of the Company or any of its Affiliates with a view to providing to such customer or Prospective Customer the services provided by the Company and its Affiliates in connection with the Business; provided, however, that the restrictions set forth in this clause (i) shall apply only to customers or Prospective Customers of the Company and its Affiliates with whom You had Material Contact (as defined below) during the twelve (12)-month period immediately preceding the termination of Your employment with the Company and its Affiliates, or (ii) induce or attempt to induce any customer or licensee of the Company or any of its Affiliates to cease doing business with the Company or such Affiliate (including, without limitation, by making any negative or disparaging statements or communications regarding the Company or its Affiliates). As used herein, "Prospective Customer" shall mean any Person to whom the Company or any of its Affiliates has sent or delivered a written servicing proposal or contract in connection with the Business of the Company and its Affiliates, and "Material Contact" shall mean contact between You and each customer or Prospective Customer (A) with whom You dealt; (B) whose dealings with the Company were coordinated or supervised by You; or (C) about whom You obtained Confidential Information in the ordinary course of business as a result of Your association with the Company.

**9. Employee Non-Solicitation.** You agree that during Your employment with the Company and for a period of twelve (12) months after termination of Your employment with the Company for any reason, You will not directly or indirectly through another person or entity, except on behalf of the Company, recruit, hire or attempt to recruit or hire, directly or by assisting others, any other person who was an employee of the Company or any of its Affiliates within the two-year period prior to Your termination of employment or is an employee of the Company or any of its Affiliates following Your termination of employment, or otherwise induce or attempt to induce any employee of the Company or any Affiliate to leave the employ of the Company or such Affiliate or in any way interfere with the relationship between the Company or any Affiliate and any employee thereof.

**10. Termination of Restrictive Covenants.** In the event of a winding-up, dissolution or general cessation of business by the Company, or the Company's failure to make the severance payments provided under Section 4(b) hereunder which continues uncured for more than 90 days, the covenants set forth in Sections 7, 8 and 9 shall automatically terminate.

**11. Enforcement.** If, at the time of enforcement of Sections 5, 6, 7, 8 or 9 of this Agreement, a court holds that the restrictions stated herein are unreasonable under circumstances then existing, the parties hereto agree that the maximum period, scope or geographical area reasonable under such circumstances shall be substituted for the stated period, scope or area and that the court shall be allowed to revise the restrictions contained herein to cover the maximum period, scope and area permitted by law. You agree that the covenants contained in Sections 5, 6, 7, 8 and 9 are of the essence of this Agreement; that each of the covenants is reasonable and necessary to protect the business, interest and properties of the Company; and that irreparable loss and damage will be suffered by the Company should You breach any of the covenants. Therefore, You agree that in addition to all other remedies provided by law or in equity, the Company and its Affiliates or their successors and assigns shall be entitled to a temporary restraining order and temporary and permanent injunction to prevent a breach or contemplated breach of any of the covenants (without posting a bond or other security). In addition, in the event of a breach or violation by You of Section 7, the time period set forth therein shall be automatically extended by the amount of time between the initial occurrence of the breach or violation and when such breach or violation has been duly cured. You acknowledge that the restrictions contained in Section 7 are reasonable and that You have reviewed the provisions of this Agreement with Your legal counsel.

**12. Additional Acknowledgments.** You acknowledge that the provisions of Sections 5, 6, 7, 8 or 9 are in consideration of: (i) employment with the Company, and (ii) additional good and valuable consideration as set forth in this Agreement. In addition, You agree and acknowledge that the restrictions contained in Sections 5, 6, 7, 8 or 9 do not preclude You from earning a livelihood, nor do they unreasonably impose limitations on Your ability to earn a living. In addition, You acknowledge (i) that the business of the Company and its Affiliates may be national in scope, (ii) notwithstanding the state of incorporation or principal office of the Company or residence of any of its respective employees (including You), it is expected that the Company and its Affiliates will have business activities and have valuable business relationships within its industry throughout the United States. You agree and acknowledge that the potential harm to the Company and its Affiliates of the non-enforcement of Sections 5, 6, 7, 8 or 9 outweighs any potential harm to You of its enforcement by injunction or otherwise. You acknowledge that You have carefully read this Agreement and have given careful consideration to the restraints imposed upon You by this Agreement, and are in full accord as to their necessity for the reasonable and proper protection of confidential and proprietary information and relationships of the Company and its Affiliates now existing or to be developed in the future. You expressly acknowledge and agree that each and every restraint imposed by this Agreement is reasonable with respect to subject matter, time period and geographical area.

**13. Representations.** You hereby represent and warrant to the Company that (i) the execution, delivery and performance of this Agreement by You does not and shall not conflict with, breach, violate or cause a default under any contract, agreement, instrument, order, judgment or decree to which You are a party or by which You are bound, (ii) You are not a party to or bound by any employment agreement with any other person or entity or any noncompete agreement or confidentiality agreement that are violated by the execution of and performance under this agreement and (iii) upon the execution and delivery of this Agreement by the Company, this Agreement shall be Your valid and binding obligation, enforceable against You in accordance with its terms. You hereby acknowledge and represent that You have consulted with independent legal counsel regarding Your rights and obligations under this Agreement and that You fully understand the terms and conditions contained herein.

**14. Corporate Opportunity.** During the Employment Period, You shall submit to the Board all business, commercial and investment opportunities or offers presented to You or of which You become aware which relate to the Business at any time during the Employment Period ("Corporate Opportunities"). Unless approved by the Board, You shall not accept or pursue, directly or indirectly, any Corporate Opportunities on Your own behalf.

**15. Cooperation.** During the Employment Period and thereafter during the Severance Period, You agree to cooperate with the Company and its Affiliates in any internal investigation, any administrative, regulatory or judicial investigation or proceeding or any dispute with a third party as reasonably requested by the Company (including, without limitation, being available to the Company upon reasonable notice for interviews and factual investigations, appearing at the Company's request to give testimony without requiring service of a subpoena or other legal process, volunteering to the Company all pertinent information and turning over to the Company all relevant documents which are or may come into Your possession, all at times and on schedules that are not disruptive of Your other permitted activities and commitments, which may include full-time employment to a future employer). In the event the Company requires Your cooperation in accordance with this Section 15, the Company shall reimburse You solely for reasonable expenses (including lodging and meals) upon submission of receipts, and, to the extent such cooperation requires a commitment of greater than five (5) hours per week, You shall be paid a per diem rate equal to one day of Base Salary for each day on which cooperation is requested.

**16. Survival.** Sections 1, 4 through 13 and 15 through 24, inclusive, shall survive and continue in full force in accordance with their terms notwithstanding the expiration or termination of the Employment Period.

**17. Severability.** In case any one or more of the provisions of this Agreement shall for any reason be held to be invalid, illegal or unenforceable in any respect by a court of competent jurisdiction, the validity of the remaining covenants set forth herein shall not be affected thereby.

**18. Assignment.** This Agreement is intended to bind and inure to the benefit of and be enforceable by the parties hereto and their respective heirs, successors and assigns, except that You may not assign Your rights or delegate Your duties or obligations hereunder without the prior written consent of Holdings.

**19. Notices.** Except as otherwise specifically provided herein, any notice required or permitted to be given to You pursuant to this Agreement shall be given in writing, and personally delivered or mailed to You by certified mail, return receipt requested, at the address set forth below Your signature on this Agreement or at such other address as You shall designate by written notice to the Company given in accordance with this Section 19, and any notice required or permitted to be given to the Company shall be given in writing, and personally delivered or mailed to the Company by certified mail, return receipt requested, addressed to the Company at the address set forth under the signature of the Company or at such other address as the Company shall designate by written notice to You given in accordance with this Section 19. Any notice complying with this Section 19 shall be deemed received when personally delivered or mailed to the addressee.

**20. Waiver.** The waiver by either party hereto of any breach of this Agreement by the other party hereto shall not be effective unless in writing, and no such waiver shall operate or be construed as the waiver of the same or another breach on a subsequent occasion.

**21. Governing Law.** This Agreement and the rights of the parties hereunder shall be governed by and construed in accordance with the internal laws of the State of Georgia without regard to its principles of conflicts of laws. You and the Company agree that any action or proceeding in connection with this Agreement shall be brought exclusively in a state or federal court sitting in or for Fulton County, Georgia. In any action or proceeding brought with respect to or in connection with this Agreement, You and the Company hereby irrevocably agree to submit to the jurisdiction and venue of the federal and state courts sitting in or for Fulton, County, Georgia.

**22. Beneficiary.** The covenants, terms, and provisions set forth in this Agreement shall inure to the benefit of and be enforceable by You, Your heirs, and legal representatives and by the Company and its permitted successors, assigns, and successors-in-interest, including, without limitation, any corporation, partnership, or other entity with which the Company may be merged. The Company shall require any such successor to expressly acknowledge and agree in writing to assume the Company's obligations hereunder. Except as expressly set forth herein, nothing expressed or implied in this Agreement is intended to confer, nor anything herein shall confer, upon any person other than the parties hereto any rights, remedies, obligations or liabilities whatsoever. Any payment that You are owed under this Agreement at the time of Your death shall be paid in accordance with the terms of this Agreement to Your estate.

**23. Entire Agreement.** This Agreement embodies the entire agreement of the parties hereto relating to Your employment by the Company in the capacity herein stated and, except as specifically provided herein, no provisions of any employee manual, personnel policies, Company directives or other agreement or document shall be deemed to modify the terms of this Agreement. No amendment or modification of this Agreement shall be valid or binding upon You or the Company unless made in writing and signed by the parties hereto. All prior understandings and agreements relating to Your employment by the Company, in whatever capacity, are hereby expressly terminated. The parties have participated jointly in the negotiation and drafting of this Agreement. If an ambiguity or question of intent or interpretation arises, this Agreement shall be construed as if drafted jointly by the parties and no presumption or burden of proof shall arise favoring or disfavoring any party by virtue of the authorship of any of the provisions of this Agreement.

**24. Time of the Essence.** Time is of the essence of this Agreement and each of the provisions hereof.

**25. Indemnification.** With respect to Your services as a director and officer of the Company and any of its Affiliates, the Company shall indemnify You and hold You harmless to the fullest extent permitted under the Company's articles of organization and Delaware law from and against any expenses, including legal fees, and all judgments, fines and amounts paid in settlement and reasonably incurred in connection with legal, administrative or investigative proceedings to which You are made, or threatened to be made, a party by reason of the fact You are or were a director or officer of the Company. In addition, if the Company or any of its Affiliates maintains director or officer indemnity insurance, You will be covered and insured under such policy to the same extent as similarly situated officers and directors.

**26. Section 409A Compliance.**

(a) The intent of the parties is that payments and benefits under this Agreement comply with Internal Revenue Code Section 409A and the regulations and guidance promulgated thereunder (collectively "Code Section 409A") and, accordingly, to the maximum extent permitted, this Agreement shall be interpreted to be in compliance therewith. In no event whatsoever shall the Company be liable for any additional tax, interest or penalty that may be imposed on You by Code Section 409A or damages for failing to comply with Code Section 409A.

(b) For purposes of compliance with Code Section 409A, (i) all expenses or other reimbursements under this Agreement shall be made on or prior to the last day of the taxable year following the taxable year in which such expenses were incurred by You, (ii) any right to reimbursement or in-kind benefits is not subject to liquidation or exchange for another benefit, and (iii) no such reimbursement, expenses eligible for reimbursement, or in-kind benefits provided in any taxable year shall in any way affect the expenses eligible for reimbursement, or in-kind benefits to be provided, in any other taxable year.

(c) For purposes of Code Section 409A, Your right to receive any installment payments pursuant to this Agreement shall be treated as a right to receive a series of separate and distinct payments. Whenever a payment under this Agreement specifies a payment period with reference to a number of days, the actual date of payment within the specified period shall be within the sole discretion of the Company.

(d) Notwithstanding any other provision of this Agreement to the contrary, in no event shall any payment under this Agreement that constitutes "deferred compensation" for purposes of Code Section 409A be subject to offset by any other amount unless otherwise permitted by Code Section 409A.

**[Signature Page Follows]**

IN WITNESS WHEREOF, You and the Company have executed and delivered this Agreement effective as of the date first shown above.

**THE COMPANY: YOU, THE EXECUTIVE:**

**Birch Communications, Inc.**

By: /s/ Anthony A. Tomae  
Name: Anthony A. Tomae  
Title: President and CEO

By: /s/ Kevin M. Dotts  
**Kevin M. Dotts**

*For purposes of its agreement under Section 3(a)(4) only,*

*Holdings executes this Agreement below:*

**HOLDINGS:**

**Birch Communications Holdings, Inc.**

By: /s/ R. Kirby Godsey  
Name: R. Kirby Godsey

Exhibit A

GENERAL RELEASE

I, \_\_\_\_\_, in consideration of and subject to the performance by Birch Communications, Inc., a Georgia corporation (together with its affiliates, the "Company"), of its obligations under the Executive Employment Agreement, dated as of (the "Agreement"), do hereby release and forever discharge as of the date hereof the Company and its affiliates and all present and former directors, officers, agents, representatives, employees, successors and assigns of the Company and its affiliates and the Company's direct or indirect owners (collectively, the "Released Parties") to the extent provided below.

1. I understand that any payments or benefits paid or granted to me under Section 4(b) of the Agreement represent, in part, consideration for signing this General Release and are not salary, wages or benefits to which I was already entitled. I understand and agree that I will not receive the payments and benefits specified in Section 4(b) of the Agreement unless I execute this General Release and do not revoke this General Release within the time period permitted hereafter or breach this General Release. I also acknowledge and represent that I have received all payments and benefits that I am entitled to receive (as of the date hereof) by virtue of any employment by the Company.
  
2. Except as provided in paragraph 4 below and except for the provisions of the Agreement which expressly survive the termination of my employment with the Company, I knowingly and voluntarily (for myself, my heirs, executors, administrators and assigns) release and forever discharge the Company and the other Released Parties from any and all claims, suits, controversies, actions, causes of action, cross-claims, counter-claims, demands, debts, compensatory damages, liquidated damages, punitive or exemplary damages, other damages, claims for costs and attorneys' fees, or liabilities of any nature whatsoever in law and in equity, both past and present (through the date this General Release becomes effective and enforceable) against the Company or any of the Released Parties which I, my spouse, or any of my heirs, executors, administrators or assigns, may have, to the extent that I have knowledge or could reasonably be expected to have knowledge of such matter or the facts giving rise to such matter, and which arise out of or are connected with my employment with, or my separation or termination from, the Company (including, but not limited to, any allegation, claim or violation, arising under: Title VII of the Civil Rights Act of 1964, as amended; the Civil Rights Act of 1991; the Age Discrimination in Employment Act of 1967, as amended (including the Older Workers Benefit Protection Act); the Equal Pay Act of 1963, as amended; the Americans with Disabilities Act of 1990; the Family and Medical Leave Act of 1993; the Worker Adjustment Retraining and Notification Act; any applicable Executive Order Programs; the Fair Labor Standards Act; or their state or local counterparts; or under any other federal, state or local civil or human rights law, or under any other local, state, or federal law, regulation or ordinance; or under any public policy, contract or tort, or under common law; or arising under any policies, practices or procedures of the Company; or any claim for wrongful discharge, breach of contract, infliction of emotional distress, defamation; or any claim for costs, fees, or other expenses, including attorneys' fees incurred in these matters) (all of the foregoing collectively referred to herein as the "Claims").

3. I represent that I have made no assignment or transfer of any right, claim, demand, cause of action, or other matter covered by paragraph 2 above.
4. I agree that this General Release does not waive or release any rights or claims that I may have under the Age Discrimination in Employment Act of 1967 which arise after the date I execute this General Release. I acknowledge and agree that my separation from employment with the Company in compliance with the terms of the Agreement shall not serve as the basis for any claim or action (including, without limitation, any claim under the Age Discrimination in Employment Act of 1967).
5. In signing this General Release, I acknowledge and intend that it shall be effective as a bar to each and every one of the Claims hereinabove mentioned or implied. I expressly consent that this General Release shall be given full force and effect according to each and all of its express terms and provisions. I acknowledge and agree that this waiver is an essential and material term of this General Release and that without such waiver the Company would not have agreed to the terms of the Agreement. I further agree that in the event I should bring a Claim seeking damages against the Company, or in the event I should seek to recover against the Company in any Claim brought by a governmental agency on my behalf, this General Release shall serve as a complete defense to such Claims. I further agree that I am not aware of any pending claim of the type described in paragraph 2 as of the execution of this General Release.
6. I agree that neither this General Release, nor the furnishing of the consideration for this General Release, shall be deemed or construed at any time to be an admission by the Company, any Released Party or myself of any improper or unlawful conduct.
7. I agree that I will forfeit all amounts payable by the Company pursuant to the Agreement if I challenge the validity of this General Release. I also agree that if I violate this General Release by suing the Company or the other Released Parties.
8. I agree that this General Release and the Agreement are confidential and agree not to disclose any information regarding the terms of this General Release or the Agreement, except to my immediate family and any tax, legal or other counsel I have consulted regarding the meaning or effect hereof or as required by law, and I will instruct each of the foregoing not to disclose the same to anyone.
9. I agree to reasonably cooperate with the Company in any internal investigation, any administrative, regulatory, or judicial proceeding or any dispute with a third party. I understand and agree that my cooperation may include, but not be limited to, making myself available to the Company upon reasonable notice for interviews and factual investigations; appearing at the Company's request to give testimony without requiring service of a subpoena or other legal process; volunteering to the Company pertinent information; and turning over to the Company all relevant documents which are or may come into my possession all at times and on schedules that are reasonably consistent with my other permitted activities and commitments. I understand that in the event the Company asks for my cooperation in accordance with this provision, the Company will reimburse me solely for reasonable travel expenses, (including lodging and meals), upon my submission of receipts.

10. I agree that as of the date hereof, I have returned to the Company any and all property, tangible or intangible, relating to its business, which I possessed or had control over at any time (including, but not limited to, company-provided credit cards, building or office access cards, keys, computer equipment, manuals, files, documents, records, software, customer data base and other data) and that I shall not retain any copies, compilations, extracts, excerpts, summaries or other notes of any such manuals, files, documents, records, software, customer data base or other data.
11. Notwithstanding anything in this General Release to the contrary, this General Release shall not relinquish, diminish, or in any way affect any rights or claims arising out of any breach by the Company or by any Released Party of the Agreement after the date hereof.
12. Whenever possible, each provision of this General Release shall be interpreted in, such manner as to be effective and valid under applicable law, but if any provision of this General Release is held to be invalid, illegal or unenforceable in any respect under any applicable law or rule in any jurisdiction, such invalidity, illegality or unenforceability shall not affect any other provision or any other jurisdiction, but this General Release shall be reformed, construed and enforced in such jurisdiction as if such invalid, illegal or unenforceable provision had never been contained herein.

BY SIGNING THIS GENERAL RELEASE, I REPRESENT AND AGREE THAT:

1. I HAVE READ IT CAREFULLY;
2. I UNDERSTAND ALL OF ITS TERMS AND KNOW THAT I AM GIVING UP IMPORTANT RIGHTS, INCLUDING BUT NOT LIMITED TO, RIGHTS UNDER THE AGE DISCRIMINATION IN EMPLOYMENT ACT OF 1967, AS AMENDED, TITLE VII OF THE CIVIL RIGHTS ACT OF 1964, AS AMENDED; AND THE EQUAL PAY ACT OF 1963, THE AMERICANS WITH DISABILITIES ACT OF 1990;;
3. I VOLUNTARILY CONSENT TO EVERYTHING IN IT;
4. I HAVE BEEN ADVISED TO CONSULT WITH AN ATTORNEY BEFORE EXECUTING IT AND I HAVE DONE SO OR, AFTER CAREFUL READING AND CONSIDERATION I HAVE CHOSEN NOT TO DO SO OF MY OWN VOLITION;
5. I HAVE HAD AT LEAST 21 DAYS FROM THE DATE OF MY RECEIPT OF THIS RELEASE SUBSTANTIALLY IN ITS FINAL FORM ON \_\_\_\_\_, \_\_\_\_\_ TO CONSIDER IT AND THE CHANGES MADE SINCE THE \_\_\_\_\_, \_\_\_\_\_ VERSION OF THIS RELEASE ARE NOT MATERIAL AND WILL NOT RESTART THE REQUIRED 21-DAY PERIOD;
6. THE CHANGES TO THE AGREEMENT SINCE \_\_\_\_\_, \_\_\_\_\_ EITHER ARE NOT MATERIAL OR WERE MADE AT MY REQUEST.

7. I UNDERSTAND THAT I HAVE SEVEN DAYS AFTER THE EXECUTION OF THIS RELEASE TO REVOKE IT AND THAT THIS RELEASE SHALL NOT BECOME EFFECTIVE OR ENFORCEABLE UNTIL THE REVOCATION PERIOD HAS EXPIRED;
8. I HAVE SIGNED THIS GENERAL RELEASE KNOWINGLY AND VOLUNTARILY AND WITH THE ADVICE OF ANY COUNSEL RETAINED TO ADVISE ME WITH RESPECT TO IT; AND
9. I AGREE THAT THE PROVISIONS OF THIS GENERAL RELEASE MAY NOT BE AMENDED, WAIVED, CHANGED OR MODIFIED EXCEPT BY AN INSTRUMENT IN WRITING SIGNED BY AN AUTHORIZED REPRESENTATIVE OF THE COMPANY AND BY ME.

DATE:

Exhibit B  
WORK PRODUCT

None

Exhibit C

EQUITY APPRECIATION BONUS

(a) Subject to the terms and conditions of this Exhibit C, a cash bonus, in the amount computed as set forth below, shall become payable to Executive by Holdings in reference to the value of the equity of Holdings subject to the further terms set forth below ("Equity Appreciation Bonus") on the sooner occur of (x) a Change in Control, or (y) February 6, 2021 ("Scheduled Bonus Date").

(b) As used herein, "Vesting Percentage" means as follows :

- (i) 0% if the Employment Termination Date is prior to February 6, 2019;
- (ii) 25% if the Employment Termination Date is on or after February 6, 2019, but prior to February 6, 2020;
- (iii) 50% if the Employment Termination Date is on or after February 6, 2020, but prior to February 6, 2021;
- (iv) 100% if the Employment Termination Date is not prior to February 6, 2021;

*provided, however*, the Vesting Percentage shall be increased (as applicable):

(x) to 100% if the Equity Appreciation Bonus is being paid in reference to a Change in Control which occurs prior to or on the Employment Termination Date; or

(y) in the event that Your employment terminates prior to February 6, 2021 (x) by the Company without Cause, (y) by You as a result of a Change in Circumstances or (z) by reason of Your death or Total Disability, to the Vesting Percentage that would have been attained if Your employment had continued until the first anniversary of the Employment Termination Date.

(c) The value of the equity of Holdings upon which the Equity Appreciation Bonus shall be computed hereunder (the "Holdings Equity Value"), subject to the proviso below, shall equal, in the case of the Equity Appreciation Bonus paid by reason of a Change in Control which occurs prior to or on the Employment Termination Date, the value of the equity of Holdings implied by the Change in Control transaction. Otherwise, the Holdings Equity Value shall be computed by Deloitte Transactions and Business Analytics LLP (or another independent agent mutually agreed) (the "Valuation Firm"), subject to verification by Executive, employing the same methodology as used by Deloitte Transactions and Business Analytics LLP in its valuation of the equity of Holdings computed as of December 31, 2015 in its report dated March 17, 2016 to compute the value of Holdings' equity (before the application of any discounts) of \$273,210,000 (the "2015 Report"), although using financial data in reference to the Company, and otherwise, as of the end of the calendar month immediately preceding the Bonus Date. *Provided however*, the Holdings Equity Value shall be decreased on a dollar-for-dollar basis to account for any capital contribution of cash or any asset, or the acquisition of any asset, including any business, to the extent (only) that additional equity of Holdings is issued therefor, with non-cash contributions in each case valued at the time of any such contribution or acquisition. For clarity and avoidance of doubt, You and Holdings agree as follows with respect to such valuation: (1) that You shall be permitted to discuss the components of the valuation with the Valuation Firm and to review and comment on the valuation before it is finalized; (2) that the weighting of the data in the valuation shall be the same as reflected in the 2015 Report (including, without limitation, 50% to the Discounted Cash Flow method, 30% to the Guideline Public Company method and 20% to the Guideline Transaction method); (3) that the Valuation Firm shall have discretion to change the guideline companies and the EBITDA multiple(s) used in the report (it being understood that, in all cases, the determination of the Valuation Firm shall, absent manifest error, be final, binding and conclusive); and (4) that, in the event that there shall be created a New Holding Company, the calculations set forth herein shall be of the value of the equity of New Holding Company, not Holdings, and will include the assets and liabilities of such New Holding Company and its Affiliates, including without limitation the assets and liabilities of Holdings and of the Company and its direct and indirect subsidiaries.

(d) The Equity Appreciation Bonus shall equal the Vesting Percentage multiplied times the bonus dollar sum applicable below:

Holdings Equity Value  
 equal or exceeding but less than  
 succeeding sum  
 (dollars in millions)

Equity Base Value (EBV)	Percent earned	Cumulative Earned Equity Bonus
EBV + \$40	1%	\$400,000
EBV + \$80	1%	\$800,000
EBV + \$120	1%	\$1.2 million
EBV + \$160	1%	\$1.6 million
EBV + \$200	1%	\$2.0 million
EBV + \$240	1.5%	\$2.6 million
EBV + \$280	1.5%	\$3.2 million
EBV + \$320	1.5%	\$3.8 million
Each succeeding level - equals prior level succeeding level plus \$40	1.5%	plus \$600,000

*Provided*, should the Holdings Equity Value exceed the EBV but fall in between any of the value levels specified above, then the amount of the Equity Appreciation Bonus will equal the amount indicated for the level achieved plus a pro rated amount of the additional bonus amount (\$1 million or \$1.5 million, as the case may be) obtainable at the next highest value level. For example, if the Holdings Equity Value is EBV + \$20 million, the Equity Appreciation Bonus will be \$1.5 million, and if EBV + \$130 million, it will be \$4.25 million.

As used herein, EBV means the value of the equity of Holdings which was computed by Deloitte Transactions and Business Analytics LLP as of December 31, 2015, which was dated March 17, 2016.

(e) The Equity Appreciation Bonus shall be payable, in the case of a Change in Control, coincident with the closing of such transaction, except as provided in the following section. If a portion of the consideration in respect of a Change in Control is contingent or escrowed, to the extent permitted by Treas. Reg. § 1.409A-3(i)(5)(iv), the payment of the Equity Appreciation Bonus shall be on the same schedule and under the same terms and conditions as apply to shareholders generally, provided that such payment of the Equity Appreciation Bonus will be made no later than five (5) years after the Change in Control.

(f) If the Equity Appreciation Bonus is payable in reference to the Scheduled Bonus Date, and not in respect of the occurrence of a Change in Control, it shall be paid in six (6) equal quarterly installments, payable on the last day of each calendar quarter, during the eighteen (18) months beginning with the first calendar quarter succeeding the Scheduled Bonus Date. In addition, all unpaid installments and other sums due in respect of the Equity Appreciation Bonus payable in reference to the Scheduled Bonus Date shall be paid upon the subsequent occurrence of a Change in Control. In the event of Your death following the Change in Control but prior to conclusion of Equity Bonus quarterly payments, remaining payments shall be made to Your designated beneficiary or to Your estate.

(g) The provisions of this Exhibit C shall survive any termination of employment of Executive (including by reason of death) or termination of this Agreement, subject to the particular terms and conditions of this Exhibit C.