

CYPRESS COMMUNICATIONS HOLDING CO INC

Form 10-K

April 15, 2005

**Table of Contents**

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-K**

(Mark One)

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

For the fiscal year ended December 31, 2004

**○ 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 000-30401

**CYPRESS COMMUNICATIONS HOLDING CO., INC.**

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(Exact name of registrant as specified in its charter)

|                                                       |                     |
|-------------------------------------------------------|---------------------|
| DELAWARE                                              | 36-4166222          |
| (State or other jurisdiction                          | (I.R.S. Employer    |
| of incorporation or organization)                     | Identification No.) |
| 15 PIEDMONT CENTER, SUITE 100, ATLANTA, GEORGIA 30305 |                     |

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(Address of principal executive offices) (Zip Code)  
(404) 869-2500

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(Registrant's telephone number, including area code)  
Securities registered pursuant to Section 12(b)  
of the Act :

| Title of each class | Name of each exchange on which<br>registered |
|---------------------|----------------------------------------------|
| None                | None                                         |

Securities registered pursuant to Section 12(g)  
of the Act :

COMMON STOCK, \$0.001 PAR VALUE

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act). Yes ☐ No ☒

The aggregate market value of the registrant's outstanding shares of common stock held by non-affiliates as of June 30, 2004 was \$2,131,595.59, computed by reference to the closing sale price of the common stock of \$0.61 per share on such date. Aggregate market value has been estimated solely for the purposes of this report. For purposes of this calculation, all executive officers, directors and 10% stockholders are classified as affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date: 6,723,395 shares of common stock as of March 1, 2005.

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**CYPRESS COMMUNICATIONS HOLDING CO., INC.**

**FISCAL YEAR 2004 FORM 10-K ANNUAL REPORT**

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**TABLE OF CONTENTS**

|                       |                                                                                                                     |           |
|-----------------------|---------------------------------------------------------------------------------------------------------------------|-----------|
| <b><u>PART I</u></b>  |                                                                                                                     | <b>1</b>  |
| <u>ITEM 1.</u>        | <u>BUSINESS</u>                                                                                                     | <b>2</b>  |
| <u>ITEM 2.</u>        | <u>PROPERTIES</u>                                                                                                   | <b>17</b> |
| <u>ITEM 3.</u>        | <u>LEGAL PROCEEDINGS</u>                                                                                            | <b>17</b> |
| <u>ITEM 4.</u>        | <u>SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS</u>                                                          | <b>18</b> |
| <b><u>PART II</u></b> |                                                                                                                     | <b>18</b> |
| <u>ITEM 5.</u>        | <u>MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES</u> | <b>18</b> |
| <u>ITEM 6.</u>        | <u>SELECTED FINANCIAL DATA</u>                                                                                      | <b>19</b> |
| <u>ITEM 7.</u>        | <u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>                        | <b>21</b> |
| <u>ITEM 7A</u>        | <u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>                        | <b>33</b> |
| <u>ITEM 8.</u>        | <u>FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA</u>                                                                  | <b>34</b> |
| <u>ITEM 9.</u>        | <u>CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE</u>                         | <b>70</b> |
| <u>ITEM 9A.</u>       | <u>CONTROLS AND PROCEDURES</u>                                                                                      | <b>70</b> |
| <u>ITEM 9B.</u>       | <u>OTHER INFORMATION</u>                                                                                            | <b>70</b> |

|                                                                                                                |    |
|----------------------------------------------------------------------------------------------------------------|----|
| <b><u>PART III</u></b>                                                                                         | 71 |
| <u>ITEM 10. DIRECTORS and EXECUTIVE OFFICERS OF THE REGISTRANT</u>                                             | 71 |
| <u>ITEM 11. EXECUTIVE COMPENSATION</u>                                                                         | 73 |
| <u>ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS</u> | 77 |
| <u>ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS</u>                                                 | 79 |
| <u>ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES</u>                                                         | 81 |
| <b><u>PART IV</u></b>                                                                                          | 81 |
| <u>ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES</u>                                                        | 82 |
| <b><u>SIGNATURES</u></b>                                                                                       | 85 |
| <u>EX-10.16 EXECUTIVE COMPENSATION ARRANGEMENTS</u>                                                            |    |
| <u>EX-10.17 DIRECTOR COMPENSATION ARRANGEMENTS</u>                                                             |    |
| <u>EX-31.1 SECTION 302 CERTIFICATION OF THE CEO</u>                                                            |    |
| <u>EX-31.2 SECTION 302 CERTIFICATION OF THE CFO</u>                                                            |    |
| <u>EX-32.1 SECTION 906 CERTIFICATION OF THE CEO</u>                                                            |    |
| <u>EX-32.2 SECTION 906 CERTIFICATION OF THE CFO</u>                                                            |    |

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**Table of Contents**

**PART I**

**SPECIAL CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS**

**(All dollar amounts are presented in thousands, except per share amounts)**

Certain statements contained in this report constitute forward-looking statements within the meaning of the United States Private Securities Litigation Reform Act of 1995. In some cases, forward-looking statements can be identified by the use of forward-looking terminology such as may, will, estimate, intend, continue, believe, expect, or the negatives thereof, variations thereon or similar terminology. These forward-looking statements are found at various places throughout this report. These forward-looking statements generally relate to estimates, plans and objectives related to future operations as well as the markets for our services and products and are based upon management's estimates of future results or trends. Although we believe that the plans and objectives reflected in or suggested by such forward-looking statements are reasonable, such plans or objectives may not be achieved. Actual results may differ from projected results due, but not limited, to assumptions which do not materialize, unforeseen developments, and/or matters beyond our control, including developments relating to the following:

the availability and adequacy of our cash flow to satisfy our obligations, including our debt service obligations, and our need for additional funds required to support capital improvements, development and acquisitions;

the consummation, or failure to consummate, the acquisition of Cypress by TechInvest Holding Company, Inc.;

recovery of the taxes and surcharges overpaid to certain telecommunications service providers;

economic, competitive, demographic, business and other conditions in our markets and with respect to our product offerings;

changes or developments in the laws, regulations or taxes in the telecommunications industry;

actions taken or omitted to be taken by third parties, including customers, suppliers, competitors, and stockholders, as well as legislative, regulatory, judicial and other governmental authorities;

the occupancy rates in the buildings in which we maintain access agreements and the rate at which customers move out of and tenants move into such buildings;

the number of persons that our customers employ;

the amount charged by telecommunications carriers to provide voice and data network elements;

changes in business strategy, capital improvements and development plans;

changes in personnel or their compensation;

an inability to renew or early termination of our contracts;

an inability to increase revenues and reduce costs in our existing operations;

an inability to engage in future acquisitions;

the loss of any license or permit;

resolution of any pending or future litigation in a manner adverse to us; and

the other factors discussed under **Risk Factors That May Affect Future Results** in Item 1 and elsewhere in this report.

You should read this report completely and with the understanding that actual future results may be materially different from what we expect. All subsequent written and oral forward-looking statements attributable to us or persons acting on our behalf are expressly qualified in their entirety by the foregoing

## **Table of Contents**

factors and the factors discussed in Item 1 and elsewhere in this report. These forward-looking statements speak only as of the date of the document in which they are made. We disclaim any obligation or undertaking to provide any updates or revisions to any forward-looking statement to reflect any change in our expectations or any change in events, conditions or circumstances on which the forward-looking statement is based, in any future statement, report, press release or other communication.

## **ITEM 1. BUSINESS**

### **INTRODUCTION**

Cypress Communications Holding Co., Inc. (together with its subsidiaries, Cypress Holding, we, us, or our ) (formerly U.S. RealTel, Inc.) operates in one business segment, namely, the provision of telecommunications services. Since Cypress Holding's acquisition of Cypress Communications, Inc. (Cypress Communications ) in February 2002, it has provided a full range of telecommunications services to small to medium sized businesses in commercial office buildings located in select major metropolitan markets in the United States. During 2001 and through the first quarter of 2002, Cypress Holding also operated in the telecommunications business rights segment, all of which operations were conducted in Latin America, namely in Argentina and Brazil. In March 2002, Cypress Holding liquidated its Latin American telecommunications rights operations. See Description of Business Discontinuance of Telecommunications Rights Business.

### **TELECOMMUNICATIONS SERVICES**

#### **Overview**

Cypress Holding, through Cypress Communications, is an on-demand communication solution provider in 25 major metropolitan U.S. markets. Each day, Cypress connects more than 100,000 employees for over 8,000 small and medium-sized businesses in commercial office buildings. As the nation's largest provider of in-building, managed communication solutions, Cypress supplies fully managed voice, data and Internet communications, including advanced digital and IP phones, unlimited local and long distance calling, business-class and dedicated Internet connectivity, firewalls, security and VPN solutions, audio/web conferencing, business television and IP communication solutions. We deliver these services over fiber optic, digital and broadband networks that we design, construct, own or lease and operate inside large and medium-sized office buildings.

We target large and medium sized commercial office buildings in central business districts and suburban office markets within select major metropolitan markets in the United States where small and medium-sized businesses are typically located. We believe that our target businesses generally are under-served by incumbent telecommunication service providers. Properties that house many tenants with heavy demand for telecommunications services are the most desirable properties and offer us the opportunity to generate the highest revenue. Our current operations are in the following 25 markets: Atlanta, Birmingham, Boston, Chicago, Dallas, Denver, Hartford, Houston, Indianapolis, Miami, Minneapolis, Nashville, New Orleans, New Jersey, New York, Orlando, Philadelphia, Phoenix, Pittsburgh, Portland, San Francisco, Seattle, Southern California (Los Angeles and Orange County), Tampa and Washington, DC.

In all of our markets we bundle voice and internet data services to provide one-stop shopping communications solutions under the service brand EZ Office Communications to building tenants at competitive prices. In 68 buildings, we also provide business class cable television services as part of our comprehensive communications package. Because we currently own or lease and operate our in-building networks, we are typically able to deploy services to a new customer within a few days of receiving an order. In addition, we are often able to provide same day service for existing customers requesting new services or features, such as increased internet bandwidth or additional

telephone lines.

Our current telecommunications services include:

2

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## **Table of Contents**

Data Services. We utilize our in-building fiber optic networks to deliver high-speed Internet access directly to our customers in approximately 20 percent of our in-service buildings. The remaining buildings are served by leased facilities with the incumbent local exchange carriers and other competitive local exchange carriers (CLEC). We also utilize in-building CATV (Category 5 Cable) to deliver high-speed Internet access directly to our customers under the service name *SmartNet* in approximately another 20 percent of our in-service buildings. The buildings which utilize fiber optic networks and CATV deliver the high-speed Internet access using a Cisco Systems router and switch deployed in the building. The remaining buildings employ high speed Internet access delivered through a Digital Subscriber Line Access Multiplexer (DSLAM) deployed in the building over twisted pair copper infrastructure. Our Internet service provides full Internet protocol routing, symmetric upstream and downstream bandwidth, and plug-and-play installation. Our customers do not need to purchase or maintain any specialized hardware to use our Internet service. Moreover, because our service is capable of delivering up to 10/100 Mbps Ethernet connectivity, we are poised to meet our customer's growing bandwidth needs. The key features of our Internet services are:

Dedicated High Speed Connectivity: Our *SmartNet* service is available with access speeds of 768kbs to 45 Mbps or more and is designed to be always on, providing instantaneous connections and the capability to receive or transmit information continuously.

Flexibility: We can usually increase a customer's bandwidth speed within minutes of receiving a request.

Diversity: We incorporate logically and physically diverse Internet circuits in our collocation facilities in each city to protect customer Internet connections from disruption.

Reliability: Each of our collocation facilities is supported by backup battery power. Moreover, we monitor all of our equipment, circuits and connections from our network operations centers in Atlanta and Norcross, Georgia. Should an outage occur in our network, we are notified immediately.

In addition to our standard Internet access service, we offer other enhanced data services, including:

E-mail, featuring IPSwitch's mail server version 7.13 and Postfix. Our service permits customers to use any e-mail client, including Microsoft Outlook, Outlook Express and Netscape Mail; access e-mail remotely using any web browser; set instant reply messages; and forward messages to supported pagers or voice e-mail systems.

Web conferencing, marketed under the *SmartConferencing* brand, offers our customers a flexible Web conferencing and virtual collaboration solution. When combined with EZ Office's audio conferencing, it transforms a phone and PC with an Internet connection into a virtual conference room, an online auditorium or an electronic brainstorming session. Employees can effortlessly meet, collaborate and exchange ideas, documents and information in real time without ever leaving their offices. With *SmartConferencing*, users benefit from a rich communication and collaboration solution involving voice, data, video, and presence.

Web site hosting, featuring Compaq Proliant Servers running Microsoft Windows 2000 Advanced Servers with IIS and Linux with Apache Servers. Our web site hosting also includes, on the Linux servers, graphs of web site hit statistics, access to a database called MySQL, PHP and PERL support.

Domain Name Registration (DNS). DNS can include all or some of the following: registration of a domain, hosting, and the ability to make DNS updates quickly with one phone call.

Network Security Solutions. We offer a fully managed, network security solution, *SmartShield* includes managed firewall, content filtering, spam blocking, Virtual Private Network (VPN) and virus protection options. *SmartShield* detects, blocks and reports on



**Table of Contents**

network security threats. Web content filtering helps to control where and when employees surf. Spam blocking stops unwanted email, before it enters the network. The SmartShield Virtual Private Network effectively secures network communications and encrypts data between offices, telecommuters and traveling employees, and continuous anti-virus protection guards against known viruses, worms, Web attacks and email intrusions.

**Monitoring Services.** We provide 24-hour monitoring of web servers, e-mail servers and customer local area networks. We can monitor customer systems every 5 minutes, 24 hours a day. If we encounter problems, we can notify our customers via e-mail, pager or both.

**NNTP Internet News Feed.** We carry a network news feed that contains over 30,000 news groups.

**Voice Services.** Substantially all of our voice services customers rent their telephone devices from us. This ensures a compatible interface with our in-building communications equipment and provides customers with a number of key benefits, including access to an advanced, multi-function digital telephone system; significant reductions in up-front capital costs; and reduced risk of technological obsolescence. Our voice offerings include both traditional telephone services, such as local and long distance services, as well as value-added services, such as integrated voicemail, audio conferencing, webconferencing, calling cards and customizable toll-free number services. Additional enhanced features include call waiting, call forwarding, dial-back and caller identification.

**Bundled Voice and Data Services.** Our customers tell us that assessing needs and selecting and managing vendors for voice, data and video communications services is becoming increasingly complex. The historical approach to selling communications services has been a la carte packaging from numerous vendors. In the fall of 2003, we introduced our EZ Office Communications suite which provides complete solutions for a simplified seat price. This bundling approach has been popular with both new and existing customers and has the potential to substantially optimize the customer buying process. We have also seen a significant trend toward flat rate or unlimited long distance packaging. We began packaging EZ Office Flat Rate solutions in the fall of 2003 and expect a majority of future customers to purchase these types of solutions.

**Voice over Internet Protocol (VoIP) Services.** In late 2003, we began offering our bundled VoIP service offering both inside and outside our 1,300 on-net office buildings. EZ Office IP Communications is a fully managed voice, data and Internet solution that combines the durability of traditional telecom with the advanced functionality of a Web-enabled user interface and innovative user features, such as:

Unified Messaging that delivers and manages voicemail using Microsoft Outlook.

Remote office capability that allows a home phone, cell phone or hotel phone to be used as a business phone.

Simplified dialing and common functionality across multiple locations.

Softphone for point-and-click dialing at the desktop.

Attendant Soft Console for advanced, centralized call handling.

Call center queuing, basic IVR, reports and agent interface.

Virtual numbers for a local number presence anywhere in the United States.

Customizable Music-On-Hold.

Audio and Web conferencing for real-time collaboration.

We launched the EZ Office IP Communications service offerings in mid-2004 to all of our 25 markets, which enables our VoIP solutions over our high speed Internet service. The specific application for delivering voice communications features to end-users is known as IP Centrex. IP Centrex can enable significant new functionality for our customers and is expected to be the next wave of communications solutions for business customers. IP Centrex can also be provided over managed local loops which

**Table of Contents**

allows us to provide services to customers in off-net buildings. The benefits of IP Centrex for us include opportunities to:

Follow customers if they move out of our current buildings.

Sell new services to existing customers.

Compete for customers that want a common solution for multiple locations.

Obtain customers that want the latest in technology.

Sell to customers in almost any building.

Our VoIP solution consists of our EZ Office Web Dashboard, unlimited local calling, bundled minutes or unlimited long distance, high speed Internet and Cisco IP telephones. Functionality includes:

IP Phones. To date, we have provided IP phones from Cisco, but there are other potential providers in this market. IP phones provide the traditional telephone features as well as the flexibility to plug the phone into a standard Ethernet connection at the office or home. Cisco has sold over 2.5 million IP phones and is a leader in the market. IP phones permit software updates to be uploaded to provide patches and enhancements that are not possible on traditional phones.

Find Me. Provides the ability to control the routing of your incoming calls. Establishes one number for all your phones (office, cell, home office). Manages important calls and blocks calls as your business needs change.

Visual Voicemail. Accesses and manages your voicemail just like email from your laptop or desktop PC, which we believe is much easier to utilize than the traditional method of using the keypad on a telephone.

Unified Messaging. Delivers voicemails to your email inbox (such as Outlook) and attaches voicemail messages to emails.

Call Logs. Displays all received, missed and dialed calls for last 90 days. Allows for simple click to call dialing, even when you are traveling.

Instant Conferencing. Lets you join 2-10 people instantly from any Internet connection.

Scheduled Conferencing. Allows you to establish a scheduled conference call for several participants with advanced functionality to manage the call.

Company Private Instant Messaging. Allows employees to chat with each other without the distractions of more commonly available instant messaging solutions.

Soft Console. Allows users to determine each employees availability status, even if they are remote.

Management Console. Provides simple administration from a web interface for set-up and changes.

Video and Other Services. In 68 buildings, we offer our customers a comprehensive package of business class television services consisting of news, business, sports and network programming. We deliver these services directly to our customers over our in-building networks using a combination of direct broadcast satellite programming and off-air local channels. Our customers can elect to receive more or less programming depending on their needs.

We continue to investigate, test and add, where appropriate, complementary communications products and services to enhance our one-stop shopping strategy.

## **Table of Contents**

### **Employees**

As of March 1, 2005 we employed 331 active, full-time employees, all in the United States. All of these employees are employed by Cypress Holding's wholly-owned subsidiary, Cypress Communications. We believe our employee relationships are good.

### **Competition**

We face significant competition. Both existing competitors and numerous other companies that may seek to enter one or more aspects of our businesses may expose us to severe price competition for our services and for building access rights. Many of our competitors have significantly greater financial resources and may also be able to respond more quickly to technological developments and changes in customers' needs.

We face competition in providing telecommunications services from:

**In-Building Communications Providers.** Because our license agreements are generally non-exclusive, substantially all of the landlords of the buildings in which we provide services are free to grant access, sales and marketing rights to one or more of our competitors. It is not yet clear whether it will be profitable for two or more companies to operate in-building networks within the same property. We are the only in-building provider in most of the buildings in which we operate, however, there is no assurance that this will continue to be the case in the future.

**Local Telephone Companies.** Incumbent local telephone companies ( ILECs ) have several competitive strengths, including established brand names and reputations, and sufficient capital resources to rapidly deploy or expand communications equipment and networks. Although these companies had been limited until recently to offering local services, they now are authorized to provide long distance service in all states, enabling them to offer "one-stop shopping" for communications services in competition with us. Recently, SBC Communications has entered into an agreement to acquire AT&T Communications; and Verizon Communications has entered into an agreement to acquire MCI Communications. If these mergers are consummated, other ILECs are likely to acquire nationwide and worldwide network assets, and these companies will evolve from "local" telephone companies into integrated, global telecommunications enterprises, which will magnify the competitive strengths they already enjoy. Many CLECs market retail services and selectively construct in-building facilities within our licensed buildings. ILEC dominance, and the more limited competition presented by CLECs, diminishes our opportunity to provide competitive local exchange services and may necessitate reductions in, or shrink potential margins from, our voice operations generally.

**Long Distance Companies.** Many of the leading long distance companies, such as AT&T, MCI and Sprint, have the capacity to build their own in-building voice and data networks. Other national long distance carriers, such as Level 3, Qwest and Williams Communications, are building and managing high speed, fiber-based, national voice and data networks, and such companies may extend their networks by installing in-building facilities and equipment. As noted above, the traditional boundaries between local and long-distance providers are increasingly blurred, resulting in greater competition in all forms of voice communications services.

**Internet Service Providers.** Internet service providers, such as Earthlink, Prodigy, Sprint and the UUNet subsidiary of MCI, provide traditional and high-speed internet access to residential and business customers, generally using existing communications infrastructure.

Digital Subscriber Line Companies. Digital subscriber line companies and/or their internet service provider customers, such as Covad, AT&T and various RBOC affiliates, provide high capacity internet access using digital subscriber line technology, which enables data



## **Table of Contents**

traffic to be transmitted over standard copper telephone lines at much higher speeds than these lines would normally allow.

**Cable-based Service Providers.** Cable-based service providers use cable television distribution systems to provide high capacity Internet access and video services.

**VoIP/ IP Centrex Providers.** National Retail IP Centrex providers such as ICG and MCI Advantage have competitive offerings today and may become more aggressive in the marketplace. Wholesale providers such as Level 3 and GoBeam are expected to partner with numerous national retail channels which could include RBOCs and long distance companies. IP-PBX providers such as Cisco, Avaya, Nortel, Shoreline, Siemens and others are competing for PBX upgrades and multi-site networks which would compete for, or replace, our offerings. Network-only providers such as Cbeyond are using low cost VoIP networks to package bundles of local/ long distance and Internet services in competition to our offerings. Stand alone VoIP application providers like Vonage also market their services to small business customers in competition with us, and larger companies such as AT&T and Verizon have started to enter this market as well. IP Phone providers likely will grow and could offer both phone and service solutions in competition to our offerings. It is expected that most telecommunications service providers will deploy VoIP services of some kind either directly or through partnerships. There are still many issues with integration, standardization, OSS systems, operational support and other areas that make building your own network very complex. We expect numerous acquisitions to reshape the industry players. For example, GoBeam recently announced merger with Covad. The VoIP market is in the early stages and is rapidly evolving.

## **Sales and Marketing**

We market our on-net telecommunications services directly to the tenants in our licensed buildings. Our typical license agreement enables us to display and disseminate our marketing materials in the leasing office and other locations within a building. Many of our license agreements also require building owners, along with management and leasing representatives to advise tenants of the availability of our services and notify us as new tenants enter the building. In addition to these rights, we use landlord, property manager and tenant testimonials and references as marketing tools. We currently provide data and/or voice communications services to many of the landlords and property managers within our licensed buildings, due in part to the requirement under some of our license agreements that we provide free basic Internet access to such parties.

Our VoIP based EZ Office Communications Suite allows us to utilize leased, high speed data facilities to connect to any commercial customers premises in our 25 major metropolitan markets. This bundled EZ Office IP Communications offering effectively expands our addressable market for deploying bundles services outside of our traditional 1,000 on-net buildings.

Our sales approach is highly consultative. In our initial sales meetings, we work closely with prospective customers to assess their particular communications needs. We then present potential customers with customized proposals which we believe are often less expensive, more comprehensive and easier to administer than their current communications solutions.

## **Real Estate Selection and Marketing**

Overall, as of December 31, 2004, we had license agreements giving us the right to operate our networks in more than 1,500 buildings, representing more than 500 million rentable square feet of office space in the United States and we were actually operating in approximately 1,000 of those buildings, representing more than 300 million rentable square feet of office space. Under the terms of our license agreements, we pay property owners a fixed rental fee and/or a percentage of the revenue we receive from providing communications services to the tenants in a building.



## **Table of Contents**

### **Suppliers**

We connect our in-building networks to local, long distance and Internet service providers in order to serve our customers. In most of our markets, we connect our networks to, and lease facilities from, CLECs, collocation service providers and local telephone companies.

We purchase long-distance transmission capacity from several long-distance carriers, such as MCI, XO Communications and AT&T. Under some of these agreements, we are required to undertake material minimum revenue and/or volume commitments. For a description of our aggregate commitments see Note 9(c) to the Notes to our Consolidated Financial Statements.

To provide Internet services to our customers, we purchase intraLATA data transmission connectivity between our licensed buildings and local points of presence from CLECs, including MCI, XO Communications, Time Warner Telecom and local exchange carriers. We obtain our local points of presence from collocation service providers, such as C3 Communications, IX2, Semaphore and Switch & Data. We use broadband service providers, such as MCI, XO Communications, Level 3 and Sprint, to procure connectivity between our collocation facilities and the Internet backbone.

Our in-building networks contain equipment such as data switches and routers, voice switches and other communications and video equipment that we purchase from Nortel Networks, Cisco Systems, Viadux and other manufacturers. As of March 1, 2005, we do not have minimum purchase commitments with any of our equipment manufacturers. There are alternative vendors available to us for all the types of equipment that we purchase.

### **Regulation**

*Overview.* Our telecommunications services are subject to regulation at the federal, state and local levels. The regulations that apply to our operations are susceptible to change as a result of ongoing administrative proceedings, litigation and new legislation. For example, the FCC has had a pending proceeding for several years that could result in new rules affecting our competitive position in multiple tenant environments ( MTEs ), such as limiting the preferences that landlords may allow to an in-building provider. In addition, our costs are affected by regulations governing the dominant local telephone companies, on which we rely for transmission facilities and network access in many cases. The outcome of these various proceedings, as well as any other regulatory initiatives, cannot be predicted. Future regulatory changes may have a material adverse affect on our business and operations.

*Local Voice Telephone Service.* Cypress Communications Operating Company, LLC (formerly Cypress Communications Operating Company, Inc., Cypress Operating Company ), a wholly owned subsidiary of Cypress Communications, is authorized to provide local exchange service as a CLEC in Alabama, Arizona, California, Colorado, Connecticut, Delaware, Florida, Georgia, Illinois, Indiana, Louisiana, Maryland, Massachusetts, Minnesota, New Jersey, New York, Oregon, Pennsylvania, Tennessee, Texas, Utah, Washington and Washington, D.C. Another subsidiary of Cypress Communications, Cypress Communications Holding Company of Virginia, LLC (formerly Cypress Communications Holding Company of Virginia, Inc., Cypress Virginia ), is authorized to provide local exchange service in Virginia. As a CLEC, Cypress (including both Cypress Operating Company and Cypress Virginia) is authorized to resell other carriers' local voice services. If Cypress obtains such services from ILECs, the tariff rates under which it obtains services may be subject to change as the result of regulatory proceedings over which Cypress does not have control. Depending on state regulations, Cypress may also construct its own facilities or purchase network elements from ILECs in order to provide telecommunications services. To provide local voice services as a CLEC, Cypress obtains interconnection services from an ILEC under the ILEC's existing tariff or by separate interconnection agreement. Cypress has entered into interconnection agreements with the dominant ILECs in each of the markets in which it operates.

Regulations promulgated by the FCC under the Telecommunications Act of 1996 Act (the 1996 Act ) require ILECs to provide interconnection, including access to unbundled network elements and retail

**Table of Contents**

services, at wholesale rates to CLEC competitors. Cypress has exercised its rights under the 1996 Act to obtain access to unbundled elements of the ILECs' networks in several of its markets. By doing this, as well as by migrating circuits to other CLECs, we have been able to reduce our network operating costs. These cost savings, however, depend on the regulatory duties of ILECs to provide us with unbundled elements at regulated rates. Because the regulatory duties of ILECs are subject to change, we cannot assure you that we can continue to benefit from cost savings in the future.

The FCC has revised its interconnection regulations several times since 1996 and many of the FCC's decisions have been subject to court appeals. During 2004 and early 2005, the FCC released significant changes to its rules governing access to unbundled network elements, and proposed additional changes (which have not yet been adopted) to its rules governing the prices for these elements. The FCC rules are currently the subject of appeals before the U.S. Court of Appeals in several circuits. The uncertainty from this and other pending judicial and regulatory proceedings makes it difficult to predict whether we will be able to rely on existing interconnection rights and obligations or have the ability to negotiate acceptable interconnection agreements in the future.

CLECs' local and in-state telecommunications services are typically subject to some degree of state regulation. Most states require that CLECs receive approval to operate from the state's public service commission. CLECs are generally required to file tariffs setting forth the terms, conditions and prices for voice services. In addition, under federal law, including the 1996 Act, CLECs are subject to additional obligations, including requirements to interconnect with other carriers, to provide other carriers access to their networks, to comply with number portability and dialing parity obligations, and to make the terms of their agreements available to other carriers on a non-discriminatory basis. On the other hand, CLECs have the right, among other things, to obtain interconnection with ILECs, to receive reciprocal compensation for terminating the calls of other local carriers and access charges for originating and terminating long distance calls for other long distance providers, and to purchase unbundled network elements and wholesale services of the ILEC's network at prices not available to other ILEC customers.

As a CLEC, we are required to comply with a variety of state laws and regulations concerning billing format, notices to customers, restrictions on disconnection for non-payment and other causes, filing of tariffs and reports, and payment of taxes, fees, and surcharges, including the federally-mandated universal service fund contribution. Compliance with these legal requirements increases the cost of our operations. In addition, complaints by customers or by state regulatory agencies alleging violations of any of these requirements could cause us to incur substantial legal and administrative expenses and adversely affect our business, even if the allegations are not ultimately proven.

If we construct facilities that cross public rights-of-way, for example to connect customers in two or more buildings, or to connect to the facilities of an ILEC, we may also be subject to local government land use and franchise regulations. If local governments impose conditions on granting permits or other authorizations or if they fail to grant such permits or other authorizations in a timely manner, it may negatively impact our ability to expand our network on a timely basis and adversely affect our business.

*Long Distance Voice Services.* Under current regulations, we are not required to file tariffs with the FCC in order to provide domestic interstate and international long distance services; but we are required to adhere to certain basic rules and regulations regarding such services that are promulgated by the FCC, including the payment of certain regulatory fees. Cypress Operating Company is authorized by the FCC to provide international switched resale services. In some states, we must obtain authorization to provide intrastate long distance voice services. Cypress Operating Company is currently authorized to provide intrastate long distance services in Alabama, Arizona, California, Colorado, Connecticut, Delaware, Florida, Georgia, Illinois, Indiana, Kentucky, Louisiana, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Nevada, New Jersey, New York, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, Tennessee, Texas, Utah, Washington, Washington, D.C. and Wisconsin. Cypress Virginia is authorized to provide intrastate long distance services in Virginia.

*Data Services.* Our Internet and data services generally are not subject to federal, state or local regulation. Congress and some state legislatures have considered imposing taxes and other burdens on

## **Table of Contents**

Internet service providers and regulating content provided over the Internet. In addition, we may be affected by certain statutes, regulations and court cases that assess liability against Internet service providers and other on-line service providers for providing information or content across their services or equipment that violates copyright, indecency, obscenity and other laws, or is defamatory, fraudulent or tortious in nature. The FCC is now considering a variety of proposals that could impose additional burdens on some services offered over the Internet, including obligations on some or all providers of Internet access services to contribute to the cost of federal universal service programs, and additional regulation of services that transmit voice communications over the Internet. Future regulation may have a negative impact on our ability to offer Internet services at competitive and profitable rates.

*Video and Other Services.* Our video services are regulated to a far lesser extent than the video services of traditional cable operators, which receive franchises from the municipalities they serve and typically construct facilities across public rights of way. For example, our video programming rates are not regulated and we are not subject to must carry obligations, which require cable license franchisees to provide certain programming to customers. We are subject to some technical requirements with regard to our provision of video services, such as requirements that our facilities not cause harmful interference with certain other communications systems.

We do not own or operate any direct broadcast satellites ( DBS ) or hold any similar types of licenses. Rather, we resell the programming services of DBS providers, such as DirecTV, Inc. Thus, our video services are regulated to a far lesser extent than the video services of traditional DBS operators.

Recent rulings of the FCC may help facilitate the provision of our video services. For example, the FCC has ruled that under certain circumstances, a roof may be considered an area controlled by a tenant upon which the owners of multiple unit premises cannot forbid the installation of some communication devices, such as satellite dishes.

We do not hold any cellular or similar types of radio licenses. To the extent that we provide cellular or paging services, we rent or sell pagers and wireless phones and resell the services of third party wireless providers. Consequently, while we do pay some regulatory fees, we generally are not subject to federal regulation with respect to these services.

*911 and Enhanced 911.* The FCC requires telecommunications carriers to establish 911 service, *i.e.*, three digit dialing access to public safety call centers for emergency services. Enhanced 911, or E911, service permits the public safety call center to identify a caller's telephone number and calling location for the dispatch of emergency personnel. 911 and E911 services are regulated at the federal, state and local level. Some states have enacted, or are likely to enact, legislation that will impose a penalty or surcharge on service providers whose telecommunications equipment does not meet or exceed the E911 requirements for the applicable jurisdiction. We currently offer, or are preparing to offer, 911 or E911 services in locations where the service is technically feasible; however, our ability to provide emergency service may be impeded by failed systems, systems that were not properly configured, systems that were not updated to reflect changes in technology or public networks, and certain other technical problems. We may incur penalties, surcharges, damages or other liabilities where, and to the extent that, we cannot provide 911 or E911 service.

## **Intellectual Property**

We regard certain aspects of our products, services and technology as proprietary; however, because we are not currently prosecuting any patent, trademark or copyright applications before the United States Patent and Trademark or Copyright Office, it may be possible for third parties to copy or use some of our intellectual property without authorization. Notwithstanding the foregoing, we regularly execute confidentiality, non-disclosure and non-competition agreements with our carriers, vendors, employees and representatives, in addition to other precautions, to protect our intellectual property.





**Table of Contents**

**DISCONTINUANCE OF TELECOMMUNICATIONS RIGHTS BUSINESS**

**Overview**

In our former telecommunications rights operations, we provided site access and usage rights, which we call telecommunications rights, to telecommunications companies in Latin America. We obtained telecommunications rights from property owners under long-term, master lease agreements. Under the master leases, we received the rights to install communications infrastructure in a property and/or to provide communications services to the property's tenants. In exchange, we paid the property owner a percentage of the revenues that we received from subleasing the telecommunications rights to telecommunications companies. We conducted these operations only in Argentina and Brazil. In March 2002, we liquidated our Latin American operations.

**HISTORY**

Cypress Holding was organized in January 1997 under the name AGILE, LLC. Cypress Holding was incorporated in the State of Illinois under the name U.S. RealTel, Inc. in August 1997. In November 1997, U.S. RealTel merged with and into Admiral Two Capital Corporation and the surviving company's name was changed to U.S. RealTel, Inc. On May 8, 2000, U.S. RealTel reincorporated in the State of Delaware. U.S. RealTel, Inc. established operations in Buenos Aires, Argentina in December 1998 and in Sao Paulo, Brazil in February 2000. U.S. RealTel, Inc. conducted its Latin American operations in Argentina through RealTel de Argentina, S.A., a majority owned Argentine corporation, and in Brazil through RealTel do Brasil, S.A., a majority owned Brazilian corporation. Both Latin American operations have been liquidated. On June 16, 2004, U.S. RealTel, Inc. amended its certificate of incorporation to change its name to Cypress Communications Holding Co., Inc.

In March 2002, Cypress Holding acquired Cypress Communications, a U.S. based operation that provides a full range of telecommunications services to businesses in commercial office buildings located in select major metropolitan markets within the United States. The acquisition of Cypress Communications allowed Cypress Holding to concentrate its resources and expertise on providing premium communications services to over 2,500 small and medium sized business customers in seven major metropolitan U.S. markets: Atlanta, Boston, Chicago, Dallas, Houston, Los Angeles and Seattle.

In July 2002, through Cypress Communications, Cypress Holding completed the purchase of certain assets of Intermedia Advanced Building Networks, the shared tenant telecommunications services business of WorldCom, Inc. ( ABN/STS ). The acquired assets included all customer contracts, in-building networks and the associated building access rights, as well as the necessary employees to support such assets. The acquisition of ABN/STS allowed Cypress Communications to extend its telecommunications services operations to over 5,700 small and medium sized business customers in 25 major metropolitan U.S. markets.

In March 2003, Cypress Holding, through Cypress Communications, acquired the Southern California building-centric voice and data services business of Eureka Broadband Corporation ( Eureka ). These assets included customer contracts, as well as Eureka's in-building networks and associated building access rights. The acquisition of the Eureka assets has allowed Cypress Holding to expand its telecommunications services operations to include over 750 small and medium sized business customers in the California market.

In July 2003, Cypress Holding, through Cypress Communications, negotiated the surrender of certain assets from E-Building Solutions, Inc. ( E-Building ) in California, a building-centric data services business, to mitigate the loss resulting from E-Building's default on a \$450 note receivable due to Cypress Communications. These assets included customer contracts, as well as E-Building's in-building networks and associated building access rights.



**Table of Contents**

**Risk Factors That May Affect Future Results**

An investment in our common stock involves a high degree of risk. You should carefully consider the factors described below, in addition to those discussed elsewhere in this report, in analyzing an investment in our common stock. If any of the events described below occurs, or if any risk not identified below negatively impacts us, our business, financial condition and results of operations would likely suffer, the trading price of our common stock could fall and you could lose all or part of the money you paid for our common stock.

In addition, the following factors could cause our actual results to differ materially from those projected in our forward-looking statements, whether made in this Form 10-K, our annual or quarterly reports to shareholders, future press releases, SEC filings or orally, whether in presentations, responses to questions or otherwise. See Special Cautionary Statement Regarding Forward-Looking Statements.

*The pending acquisition of the Company might not be consummated.*

As mentioned elsewhere in this report, the Company has entered into, and the stockholders have approved, an Agreement and Plan of Merger pursuant to which the Company will merge with and into a wholly-owned subsidiary of TechInvest Holding Company, Inc., an affiliate of Arcapita, Inc., and become a wholly-owned subsidiary of TechInvest Holding Company, Inc. The consummation of the merger is subject to customary closing conditions and certain regulatory approvals, all of which have not yet been completed. The failure to consummate the merger could have a material adverse impact on our business.

*We may not be able to recover any of the telecommunications taxes and surcharges that were overpaid.*

In September 2004, management determined that the Company made payments to telecommunications service providers for federal, state and local taxes and surcharges on telecommunications services for which it might be exempt. The Company is attempting to recover these taxes and surcharges directly from the telecommunications service providers involved. Although management believes that the amount of taxes and surcharges which the Company is entitled to recover is in the range of \$1,000 to \$2,500, there is no assurance that any of the amounts will be recovered or when the amounts will be recovered, if ever.

*Our short operating history makes it difficult to predict future operating results.*

Our business was founded in January 1997. We have only operated in the telecommunications services business since February 2002. As such, we have a short operating history and limited historical financial and operating data with respect to our business. We have incurred significant cumulative operating losses and negative cash flows from operations since inception.

*We may incur operating losses in the foreseeable future.*

Although we have recently achieved profitability in our operations, there is no guarantee that we can sustain this level of profitability. Since we entered into the telecommunications services business, we have only recently reported our first operating profits from continuing operations. As a result, we will need to continue to generate significant revenue to maintain profitability, which may not occur.

*Our business model may not succeed.*

We are attempting to implement our business model in a highly competitive and fast-changing telecommunications market which makes it impossible to predict the extent to which our business model will succeed. We may continue to

make substantial capital expenditures in deploying our networks without knowing whether our business plan can be successfully executed. As a result, there is a risk that our business will fail. Additionally, our limited operating history makes it difficult to evaluate the execution of our business model thus far.

**Table of Contents**

To be successful, we must develop, market and implement the various components of our business strategy at widely accepted prices that exceed our operating expenses. Even if we execute our business model as we plan, we cannot be certain that we will ever achieve favorable operating results, profitability or generate revenues sufficient to cover our capital and operating costs.

*We have substantial debt.*

We have incurred substantial debt to date for purposes of funding our acquisitions and operations. We may use a substantial portion of our cash flow to pay principal and interest on our debt, thereby reducing the funds available for working capital, capital expenditures and other general corporate purposes, including executing our business strategy. In addition, a substantial portion of this debt will become due in the next 12 months. We may not be able to generate adequate cash flows from operations to repay this debt, or we may not be able to refinance this debt with a long term debt facility. Our inability to repay or refinance this debt could have a material negative impact on our operations.

*We must attract and retain key personnel in order to implement our business plan.*

The loss of the services of key personnel or the failure to attract additional qualified personnel as required could have a material adverse effect on our ability to sustain our business or grow. We believe that our future success will depend in large part on our ability to attract and retain qualified managerial, technical and sales personnel.

*We may not be able to grow sufficiently and manage that growth in order to be successful.*

If we are successful in implementing our business plan, our operations may expand rapidly. We believe we must grow our business in order to achieve sufficient economies of scale to operate profitably. Because the communications industry is capital intensive, rapidly evolving and subject to significant economies of scale, as a relatively small organization we are at a competitive disadvantage. The growth we must achieve to reduce that disadvantage will put a significant strain on all of our resources. We will require substantial additional capital beyond that which is currently available to us in order to finance our growth according to our current business plan. If we fail to grow rapidly or obtain additional capital, we may not be able to compete with larger, more established companies.

Furthermore, rapid expansion could place a significant strain on our management, financial and other resources. Our ability to manage future growth, if it occurs, will depend on, among other things, our ability to: (1) control expenses related to our business plan; (2) maintain responsive customer service; (3) improve existing, and implement new, billing and collections, operational support and administrative systems; and (4) expand, train and manage our employee base, in particular qualified sales, technical and managerial personnel. The failure to manage our growth effectively would impair our business and operational performance. We may not be able to maintain the quality of our operations, to control our costs, and to expand our internal management, technical, information and accounting systems in order to support our desired growth.

*We rely upon information processing systems provided by others.*

Sophisticated information processing systems are vital to our growth and our ability to achieve operating efficiencies. A failure of any of these systems would have a material adverse effect on our operations and business. In addition, there may be other systems we have not identified that are required or in need of improvement. We may also be unable to maintain and upgrade these systems as necessary.

*We must purchase voice and data transmission capacity from third parties who may be unable or unwilling to meet our requirements.*

We rely upon other communications carriers, such as local telephone companies, long distance companies and Internet service providers, to provide transmission capacity from the buildings we serve.

**Table of Contents**

Our failure to obtain adequate connections from other carriers on a timely and efficient basis could delay or impede our ability to provide services and generate revenue. Sufficient capacity or redundant capacity may not be readily available from third parties at commercially reasonable rates, if at all. Our failure to obtain sufficient redundant connectivity could result in an inability to provide service in certain buildings and service interruptions, which could in time lead to loss of customers and damage to our reputation. Additionally, many of the communications carriers we rely on for transmission capacity are also our direct competitors.

*The sector in which we operate is highly competitive, and we may not be able to compete effectively.*

The numerous companies that may seek to enter our niche may expose us to greater price competition for our services. Competition could also result in a diminution of our net revenue margins. We face competition from many communications providers with significantly greater financial resources, well-established brand names, larger customer bases and diverse strategic plans and technologies. For example, we face competition from traditional and new communications companies, including local, long distance, cable modem, Internet, digital subscriber line, fixed and mobile wireless and satellite data service providers. Intense competition has led to declining prices and margins for many communications services. We expect this trend to continue as competition intensifies in the future.

If our competitors successfully focus on our market, the intense competition could materially harm our business. To the extent these competitors are successful, we may face difficulties in building our networks and marketing our services within some of our target buildings. Because our agreements to use utility shaft space within buildings are generally not exclusive, owners of such buildings may give similar rights to our competitors. If a competitor installs a network in a building in which we operate, there will likely be substantial price competition preventing us from operating in that building profitably. In addition, we may also face severe price competition for building access rights, which could result in higher sales and marketing expenses and lower profit margins.

*We must continue to obtain license agreements with building owners and managers in order to be successful.*

Our business depends upon our ability to continue to operate our in-building networks. The failure of building owners or managers to grant or renew access rights on acceptable terms, or any deterioration in our existing relationships with building owners or managers, could harm our marketing efforts and could substantially reduce our potential customer base. Current federal and state regulations do not require building owners to make space available to us, or to do so on terms that are reasonable or nondiscriminatory. Building owners or managers may decide not to permit us to install our networks in their buildings or may elect not to renew our license agreements. Non-renewal of these agreements would reduce our revenues and we might not recover our infrastructure costs.

*Alternative technologies pose competitive threats.*

The communications industry is subject to rapid and significant technological change, such as continuing developments in digital subscriber line technology and alternative technologies for providing high-speed data communications. In addition to fiber-optic technology, there are other technologies, such as VoIP, DSL and wireless technology that provide more capacity and speed than traditional copper wire transmission technology. Our success in improving and expanding our operations and services will depend on our ability to anticipate or adapt to new technology on a timely basis. The development of new technologies or the significant penetration of alternative technologies into our target market may either reduce the demand for our services, require us to devote important capital, and human and technical resources to upgrade, reconfigure or replace our current or future technology or some combination of each of these, and consequently could have a material adverse effect on our business.

**Table of Contents**

*Retained control by our principal stockholders may create conflicts of interest.*

The concentration of ownership of our stock may have the effect of delaying, deferring or preventing a change in control, merger, consolidation, or a tender offer which could involve a premium over the price of our common stock. Currently, our executive officers, directors and greater-than-five-percent stockholders and their affiliates, in the aggregate, beneficially own a substantial percentage of the outstanding common stock (not including shares issuable upon the conversion or exercise of warrants or options). If all of these stockholders were to vote together as a group, they would have the ability to exert significant influence over our board of directors and its policies as well as other significant corporate matters such as charter and bylaw amendments and possible mergers or corporate control contests.

*Legislation and government regulation could adversely affect us.*

Many of our services are subject to federal, state and/or local regulation. If we fail to comply with all applicable regulations or experience delays in obtaining required approvals, our business could be harmed. For example, we must make regular filings in some of the states in which we operate and could be fined if we do not timely make these filings. Additionally, compliance with these regulatory requirements may be costly. We may experience delays in closing future corporate transactions, including debt and equity financings and sales of any portion of our regulated business, due to requirements to obtain regulatory approval of these transactions. Regulations governing communications services also change from time to time in ways that are difficult to predict. Such changes may harm our business by increasing competition, decreasing revenue, increasing costs, impairing our ability to offer services or otherwise. For example, the FCC could mandate that building owners give access to competitive providers of communications services.

If our interpretation of regulations applicable to our operations is incorrect, we may incur additional expenses or become subject to more stringent regulation. If our interpretations of these regulations and guidelines are incorrect, we may incur additional expenses to comply with additional regulations applicable to our operations. We also may incur significant expenses to defend ourselves against complaints by customers or other persons who claim we have violated applicable regulations, even if our interpretation of the rules is ultimately upheld by the regulatory agency.

*We have significant fixed costs.*

As of December 31, 2004, we have committed to pay approximately \$10,449 for services from other communications carriers through 2007. We will have to pay those carriers even if we do not use their services. We operate in a market that requires high fixed costs to build out our in-building networks and we therefore must have high utilization of our products and services with each building in which we operate in order to be successful. We expect that the communications needs will be in excess of the purchase requirements for the years ending December 31, 2005, 2006 and 2007.

*Our business could suffer from a reduction or interruption from our equipment suppliers.*

We purchase our equipment from various vendors. Any reduction in or interruption of deliveries from our major equipment suppliers, such as Cisco Systems and Nortel Networks, could delay our plans to install in-building networks, impair our ability to acquire or retain customers and harm our business generally. In addition, the price of the equipment we purchase may substantially increase over time, increasing the costs we pay in the future. It could take a significant period of time to establish relationships with alternative suppliers for each of our technologies and substitute their technologies into our networks.



*We must make capital expenditures before generating revenues, which may prove insufficient to justify those expenditures.*

We typically install an in-building network before we have any customers in that building. Since we generally do not solicit customers within a building until our network is in place we may not be able to

**Table of Contents**

recoup all of our expenditures within any building. Prior to generating revenues in a building, we must incur initial capital expenditures. Our expenditures will vary depending on the size of the building and whether we encounter any construction-related difficulties. After initial installation of our network, our capital expenditures continue to grow based on the extent to which we add customers within a building.

*Any acquisitions or investments we make could disrupt our business and be dilutive to our existing stockholders.*

We may consider acquisitions of, or investments in, complementary businesses, technologies, services or products from time to time. Acquisitions and investments involve numerous risks, including:

the diversion of management attention;

difficulties in assimilating the acquired business;

potential loss of key employees, particularly those of the acquired business;

difficulties in transitioning key customer relationships;

risks associated with entering markets in which we have no or limited prior experience; and

unanticipated costs.

In addition, these acquisitions or investments may result in:

dilutive issuances of equity securities;

the incurrence of debt or assumption of liabilities;

large one-time expenses; and

the creation of other intangible assets that result in significant amortization expense.

Any of these factors could materially harm our business or our operating results.

*Our networks may be vulnerable to unauthorized access which could interfere with the provision of our services.*

Our networks may be vulnerable to unauthorized access, computer viruses and other disruptive problems. Remediating the effects of computer viruses and alleviating other security problems may require interruptions, incurrence of costs and delays or cessation of service to our customers. Unauthorized access could jeopardize the security of confidential information stored in our computer systems or those of our customers, for which we could possibly be held liable. Any unauthorized access could further damage our reputation and ultimately our ability to successfully compete in our market.

*Impairment of our intellectual property rights could harm our business.*

We regard certain aspects of our products, services and technology as proprietary and attempt to protect them with legal rights, contractual rights and other methods. Despite these precautions, it may be possible for a third party to copy or otherwise obtain and use our proprietary products, services or technology without authorization, or to develop similar proprietary matter independently. If a third party were to obtain our proprietary information and we were unable to prevent them from disseminating that information or using it to our disadvantage, our business could be harmed.

*The exercise of outstanding securities may have a dilutive effect.*

We have outstanding warrants and options with exercise prices ranging from \$0.01 per share to \$10.00 per share. The exercise of these securities could have a dilutive effect with respect to holders of our

**Table of Contents**

common stock. As of March 1, 2005, the total number of shares issuable by us under outstanding warrants and options was approximately 15,103.

**ITEM 2. PROPERTIES**

| LOCATION                 | CITY             | GENERAL<br>CHARACTER                                   | SQUARE<br>FEET | ANNUAL<br>RENT | LEASE<br>EXPIRATION   |
|--------------------------|------------------|--------------------------------------------------------|----------------|----------------|-----------------------|
| Piedmont Center          | Atlanta, GA      | Principal Executive<br>Office, Cypress<br>Headquarters | 35,245         | \$ 1,142       | 2005-2007             |
| 33 N. LaSalle            | Chicago, IL      | General Office                                         | 14,283         | \$ 438         | April 30,<br>2006     |
| 160 Federal Street       | Boston, MA       | General Office                                         | 7,292          | \$ 332         | June 30, 2005         |
| 1555 Oakbrook            | Norcross, GA     | General Office /<br>Warehouse                          | 36,503         | \$ 361         | January<br>1, 2007    |
| 1525 Wilson Blvd.        | Arlington, VA    | General Office                                         | 10,175         | \$ 347         | July 31, 2007         |
| 1900 Avenue of the Stars | Los Angeles, CA  | General Office                                         | 7,065          | \$ 284         | July 31, 2007         |
| 1650 Market Street       | Philadelphia, PE | General Office                                         | 5,898          | \$ 150         | December 31,<br>2009  |
| 4851 LBJ Freeway         | Dallas, TX       | General Office                                         | 7,742          | \$ 219         | September<br>30, 2005 |
| 222 W Colinas Boulevard  | Dallas, TX       | General Office                                         | 7,928          | \$ 219         | December 31,<br>2007  |
| 1600 Broadway            | Denver, CO       | General Office                                         | 8,974          | \$ 199         | July 31, 2007         |
| One Riverway             | Houston, TX      | General Office                                         | 5,188          | \$ 127         | August 20,<br>2005    |

Cypress Holding has subleased all or part of the above offices with the exception of: 160 Federal Street, 1555 Oakbrook, 1650 Market Street, 222 W. Los Colinas and One Riverway, which Cypress Holding leases directly from the landlord.

We lease space in 30 additional commercial properties in the United States for general office purposes, network facilities, storage and warehouses, in each instance under leases that do not contain material financial obligations.

### ITEM 3. LEGAL PROCEEDINGS

We are a party to various legal proceedings that are ordinary and incidental to our business. Except as set forth below, management does not expect that any currently pending legal proceedings will have a material adverse effect on our results of operations or financial position.

With respect to our ABN/STS acquisition, on or about January 23, 2003, we filed proofs of claim in the bankruptcy cases of WorldCom, Inc. and certain of its debtor affiliates as a result of such parties' defaults under that certain Asset Purchase Agreement dated May 31, 2002 by and among Intermedia Communications, Inc., Shared Technologies Fairchild, Inc., Shared Technologies Fairfield Telecom, Inc., MCI Worldcom Communications, Inc., Worldcom, Inc., MCI-WORLDCOM Network Services, Inc. and Cypress Communications, that certain Omnibus Post-Closing Agreement dated July 16, 2002, by and among Intermedia Communications, Shared Technologies Fairchild, Shared Technologies Fairfield Telecom, MCI Worldcom Communications, Worldcom, Inc., MCI-WORLDCOM Network Services and

**Table of Contents**

Cypress Communications and certain other related ancillary documents. We filed amendments to these proofs of claim on January 29, 2004 to increase our claim to approximately \$13,900, which amended proofs of claim to include damages caused to us as a result of certain fraudulent accounting practices of the debtors (not, so far as we are aware, specific to Cypress Communications) and failure to perform required actions and other breaches of the Transaction Documents by the Debtors.

On or about October 18, 2004, the Debtors objected to the Company's proofs of claim and a hearing has been set for April 22, 2005. The Company expects that WorldCom will bring counterclaims alleging breaches by Cypress of the agreements and related ancillary documents. The Company expects such counterclaims may seek damages of approximately \$2,300, of which the Company has approximately \$1,500 currently recorded in accrued expenses. The Company cannot express an opinion as to whether a favorable or unfavorable outcome is either probable or remote or to estimate the range of any possible loss or gain that may result from the settlement of these claims. An unfavorable outcome could, under certain circumstances, result in a material adverse effect on our business, financial condition and results of operations.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

No matters were submitted during the fourth quarter of fiscal 2004 to a vote of the security holders.

**PART II**

**(All dollar and share amounts are presented in thousands, except per share amounts)**

**ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

Our common stock is quoted on the Nasdaq OTC Bulletin Board (OTCBB) under the symbol CYHI. The following table sets forth, for the periods indicated, the high and low bid quotations for the common stock, as reflected on the OTCBB. The following quotations represent inter-dealer prices without adjustment for retail markups, markdowns or commissions and may not necessarily represent actual transactions.

| PERIOD         | HIGH    | LOW     |
|----------------|---------|---------|
| 2004           |         |         |
| Fourth Quarter | \$ 1.52 | \$ 0.70 |
| Third Quarter  | 1.35    | 0.60    |
| Second Quarter | 0.90    | 0.51    |
| First Quarter  | 1.10    | 0.72    |
| 2003           |         |         |
| Fourth Quarter | \$ 1.01 | \$ 0.53 |
| Third Quarter  | 1.40    | 0.70    |
| Second Quarter | 2.00    | 1.01    |
| First Quarter  | 3.00    | 1.50    |

As of March 1, 2005, there were 109 holders of record of our common stock. We believe that there are in excess of 300 beneficial owners of our common stock.

To date, we have not declared or paid any dividends on our common stock. The payment of dividends, if any, is within the discretion of our board of directors and will depend upon our earnings,

**Table of Contents**

capital requirements and financial condition and other relevant factors. We do not intend to declare any dividends in the foreseeable future, but instead intend to retain future earnings, if any, for use in our business operations.

The following table describes the equity securities issuable as of December 31, 2004 pursuant to our equity compensation plans. For a description of our equity compensation plans see Note 10 to our consolidated financial statements.

**Equity Compensation Plan Information**

|                                                            | (a)                                                                                         | (b)                                                                         | (c)                                                                                                                                         |
|------------------------------------------------------------|---------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------|
|                                                            | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) |
| Plan Category                                              |                                                                                             |                                                                             |                                                                                                                                             |
| Equity compensation plans approved by security holders     | 3,462                                                                                       | 1.60                                                                        | 1,539                                                                                                                                       |
| Equity compensation plans not approved by security holders | 12,361                                                                                      | 1.22                                                                        |                                                                                                                                             |
| Total                                                      | 15,822                                                                                      | 1.30                                                                        | 1,539                                                                                                                                       |

**ITEM 6. SELECTED FINANCIAL DATA**

The selected consolidated financial data presented below as of and for the years ended December 31, 2004, 2003, 2002, 2001 and 2000 is derived from our audited consolidated financial statements. In late 2001, we discontinued the business of our predecessor company, U.S. RealTel, Inc. In March 2002, we liquidated the Latin America operations of U.S. RealTel, Inc. In February 2002, we completed the acquisition of Cypress Communications, and the results of our operations from that time are reflective of that business that was acquired, along with subsequent acquisitions in the same line of business. Certain expense items presented for 2000 and 2001 have been reclassified to comply with the current presentation format.



**Table of Contents**

(All dollar amounts are presented in thousands, except per share amounts)

|                                                                                                                 | For the Year Ended December 31, |            |            |            |          |
|-----------------------------------------------------------------------------------------------------------------|---------------------------------|------------|------------|------------|----------|
|                                                                                                                 | 2004                            | 2003       | 2002       | 2001       | 2000     |
| <b>Consolidated Statement of Operations Data:</b>                                                               |                                 |            |            |            |          |
| Revenues                                                                                                        | \$ 78,982                       | \$ 84,626  | \$ 51,717  | \$ 282     | \$ 1,720 |
| Direct Costs                                                                                                    | 37,927                          | 44,447     | 28,704     | 165        | 1,454    |
| Revenues Net of Direct Costs                                                                                    | 41,055                          | 40,179     | 23,013     | 117        | 266      |
| Operating Expenses                                                                                              |                                 |            |            |            |          |
| Sales and marketing                                                                                             | 2,869                           | 5,342      | 3,977      |            |          |
| General and administrative                                                                                      | 35,561                          | 37,694     | 25,789     | 3,699      | 8,221    |
| Extinguishment of liabilities and other credits                                                                 | (545)                           | (1,995)    |            |            |          |
| Stock based compensation                                                                                        | 78                              | 438        |            |            |          |
| Impairment of assets                                                                                            |                                 |            |            | 750        |          |
| Professional and investment banking fees                                                                        |                                 |            |            | 1,948      | 1,121    |
| Total Operating Expenses                                                                                        | 37,963                          | 41,479     | 29,766     | 6,397      | 9,342    |
| Other income (expense), net *                                                                                   | (2,669)                         | (2,863)    | (4,791)    | (1,956)    | 13,796   |
| Income (loss) From Continuing Operations                                                                        | 423                             | (4,163)    | (11,544)   | (8,236)    | 4,720    |
| Gain (loss) From Discontinued Operations                                                                        |                                 |            | 2,032      |            |          |
| Income (loss) before income taxes, extraordinary item and cumulative effect of changes in accounting principles | 423                             | (4,163)    | (9,512)    | (8,236)    | 4,720    |
| Income taxes                                                                                                    |                                 |            |            |            | 200      |
| Income (loss) before extraordinary item and cumulative effect of changes in accounting principles               | 423                             | (4,163)    | (9,512)    | (8,236)    | 4,520    |
| Extraordinary Item gain on acquisition                                                                          |                                 |            | 7,783      |            |          |
| Extraordinary Item loss on extinguishment of debt                                                               |                                 |            |            |            | 455      |
| Cumulative Effect of Changes in Accounting Principles                                                           |                                 |            |            |            | 1,396    |
| Net Income (Loss)                                                                                               | \$ 423                          | \$ (4,163) | \$ (1,729) | \$ (8,236) | \$ 2,669 |
| Net Income (Loss) Per Common Share                                                                              |                                 |            |            |            |          |
| Income (loss) from continuing operations                                                                        | \$ 0.07                         | \$ (0.71)  | \$ (1.95)  | \$ (1.32)  | \$ 0.70  |
| Gain (loss) from discontinued operations                                                                        |                                 |            | 0.34       |            |          |
| Extraordinary item                                                                                              |                                 |            | 1.32       |            | (0.07)   |
| Cumulative effect of changes in accounting principles                                                           |                                 |            |            |            | (0.22)   |
| Net Income (Loss) Per Common Share Basic and diluted                                                            | \$ 0.07                         | \$ (0.71)  | \$ (0.29)  | \$ (1.32)  | \$ 0.41  |
| Weighted Average Common Shares Outstanding                                                                      | 5,874                           | 5,874      | 5,894      | 6,246      | 6,462    |

**Table of Contents****December 31,  
(In thousands)**

|                                            | <b>2004</b> | <b>2003</b> | <b>2002</b> | <b>2001</b> | <b>2000</b> |
|--------------------------------------------|-------------|-------------|-------------|-------------|-------------|
| <b>Consolidated Balance Sheet Data:</b>    |             |             |             |             |             |
| Cash and cash equivalents                  | \$ 215      | \$ 1,900    | \$ 8,258    | \$ 2,061    | \$ 9,425    |
| Working Capital (Deficit)                  | \$ (14,213) | \$ (9,347)  | \$ (5,498)  | \$ 1,672    | \$ 8,720    |
| Total Assets                               | \$ 31,939   | \$ 35,595   | \$ 41,463   | \$ 2,382    | \$ 10,008   |
| Total long-term lease obligations and debt | \$ 10,463   | \$ 17,543   | \$ 16,173   | \$          | \$          |
| Shareholders' equity (deficit)             | \$ (1,926)  | \$ (2,433)  | \$ 1,292    | \$ 1,680    | \$ 7,097    |

\* Other income (expense), net consists primarily of interest expense, interest income and gain or loss from disposition of assets in the ordinary course of our business for the years ended December 31, 2004, 2003 and 2002. In addition to the above, other income (expense), net includes an exchange loss of \$2,145 and net gain on the sale of our North American operations of \$15,533 for the years ended December 31, 2001 and 2000 respectively.

**ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**(All dollar and share amounts are presented in thousands, except per share amounts)**

*The following Management's Discussion and Analysis of Financial Condition and Results of Operations contains forward-looking statements, which involve risks and uncertainties. Actual results could differ materially from those anticipated in these forward-looking statements as a result of certain risk factors, including those set forth under Risk Factors That May Affect Future Results below and elsewhere in this report. The following discussion also should be read in conjunction with the information set forth in our consolidated financial statements and notes thereto included in Item 8. Financial Statements of this Annual Report on Form 10-K.*

Beginning in February 2002 with Cypress Holding's acquisition of Cypress Communications, we have provided a full range of reliable, feature rich, integrated telecommunications services to businesses located in select major metropolitan markets within the United States. We are the preferred communications provider in over 1,000 Class A commercial office buildings in such select markets. Our telecommunications services include high speed Internet access and data services, local and long-distance voice services, digital telephone systems, digital satellite business television, voicemail, e-mail, web site hosting, security/monitoring services, and other advanced communications services. We deliver these services over fiber optic, digital and broadband networks that we design, construct, own or lease and operate inside large and medium-sized office buildings. Additionally, during the three month period ended March 31, 2002, we provided, or sought to provide, site access and usage rights to telecommunications companies in Latin America through our 71%-owned Argentinean subsidiary and our 89%-owned Brazilian subsidiary. In March 2002, we liquidated our Latin American telecommunications rights operations.

The year ended December 31, 2004 was the first year in which we reported net income from continuing operations exclusive of one time gains. Otherwise, except for a net gain of approximately \$15,500 on the sale of our old North American telecommunications rights operations in December 2000 and an extraordinary gain of approximately \$7,900 on the acquisition of Cypress Communications, under purchase accounting, we have incurred significant operating losses and experienced negative cash flows from operations since inception. Net income for the fiscal year ended December 31, 2004 was \$423, compared with a net loss for the fiscal year ended December 31, 2003 of \$4,163 and a net loss of \$1,729 for the fiscal year ended December 31, 2002. As of December 31, 2004, we had cash and cash

equivalents of \$215.

## **Table of Contents**

The Consolidated Statements of Operations for the fiscal year ended December 31, 2002 include operations of Cypress Communications from February 1, 2002, the date of its acquisition for accounting purposes.

### **Executive Summary**

In evaluating our financial condition, management focuses on several key themes and indicators of both revenues and expense as described below:

#### **Revenue**

The key areas of management focus relative to our revenues revolve around the status of our customer base. We provide our services generally to tenants resident within the approximately 1,300 office buildings in which we maintain access agreements. These tenants are generally operating under the terms of multi-year lease agreements with the building landlord. To the extent tenants who are our customers leave these buildings either during the term of or at the termination of their lease agreements, they may cease to be our customer. We endeavor to replace these lost customers with new tenants entering the buildings. We expend significant effort in determining the status and intentions of our existing customers relative to their current lease agreements within buildings we serve, as well as the status of prospective tenants who may be moving into these buildings.

In addition to move in move out activity, the other key revenue focus area within our customer base is the average number of users per customer. This factor is significant in determining and forecasting the average revenue per customer, and is directly tied to overall employment factors within the general economy. To the extent an existing customer hires additional employees, our revenue from that customer should generally increase. Conversely, reductions in employment totals of a customer would result in a reduction in revenue from the customer.

During 2002, 2003 and 2004, we determined that, within our retained customer base, there was an overall reduction in the number of contracted users of our services in excess of new customers added, resulting in a reduction in the average revenue per customer for our services. The rate of decline within the customer base appears to have decreased starting in the second half of 2004 with the overall improvements in the general economy.

Based on discussions with building owners in the markets we service and overall industry reports, we expect an improvement in the occupancy rates for the types of buildings that we serve in 2005. Improvement in occupancy rates in these buildings increases the number of potential sales opportunities for our services. Management believes that recent stabilization in the general employment picture in the United States will result in a stabilization or improvement in the average revenue per customer over what we are now experiencing. Additionally, the addition during 2004 of our EZ Office IP Communications service offering allows us to expand our reach to customers outside of our serviced buildings. We expect that offering to begin generating significant new customer activity starting in 2005.

#### **Costs**

One of the most significant cost elements for us is the amounts paid to telecommunications carriers for the provision of our voice and data network elements. These costs have both fixed and variable components. A key focus of management's attention is the proper management of these cost elements.

Management's objectives in managing the voice and data network elements is to provide a cost effective and highly reliable solution for our business. Achieving this objective involves determining both the correct number of circuit elements necessary to provide an appropriate level of customer service, along with determining the best cost provider for those circuit elements.



## **Table of Contents**

Starting in late 2002 and throughout 2003 and 2004, management expended considerable effort in analyzing our network on a building by building basis to optimize the combination of service and cost. We were successful in reducing our overall network costs as a percentage of revenues from year to year, while continuing to provide an appropriate level of service to our customers.

During 2003, we substantially completed a process of obtaining certification to be a CLEC in most of the markets where we operate. CLEC certification allows us to enter into agreements with the incumbent local exchange carriers ( ILECs ) to obtain network services at rates generally lower than those we previously paid. Starting in late 2003, we began the process of converting our network to the lower rate platforms with the various ILEC providers. This process was completed in early 2004 and was a significant contributor to the overall reduction in the cost of network elements during the year.

The process of network analysis and re-grooming is ongoing. Management believes that there are additional opportunities for reduction in network costs through either reduction in network elements or transfer of elements to lower cost providers.

### **Liquidity and Capital Resources**

Our primary sources of liquidity have been proceeds from the issuance of our common stock, convertible debentures, lines of credit and bridge loans, as well as proceeds from the sale of our former North American telecommunications rights operations in December 2000 and cash acquired through our acquisition of Cypress Communications. The terms of certain of our indebtedness limit our ability to incur additional indebtedness, pay dividends or undertake certain other transactions. We have also pledged certain assets as security under our senior credit facility. We must devote a substantial portion of our cash flow to service our indebtedness and cannot utilize that cash flow for operations.

Beginning in the first quarter of 2002 and continuing throughout 2003 and 2004, we initiated certain actions intended to improve liquidity and operating results. As a result, we began to realize improvement to our overall liquidity. As a result, our management believes that our cash position, net of short term borrowings, should improve during the following quarters, however, there is no assurance this will be the case.

As noted in the accompanying financial statements, we have Bridge Loan debt and fees totaling \$8,480 which will come due in July 2005. At present, we have not initiated a process to refinance this debt, pending the proposed acquisition of the Company as discussed below. If the acquisition is not consummated prior to July 2005, we would be required to either renegotiate the terms of the Bridge Loan with the current debt holders, or seek replacement financing. Our inability to renegotiate the terms of the bridge loan, or find replacement financing would have a serious negative financial impact on the Company's liquidity and ability to finance its operations. As a result of the aforementioned factors and related uncertainties, there is substantial doubt about the Company's ability to continue as a going concern.

Our liquidity and capital resources remain a focal point of our management's attention.

### **Asset Acquisitions**

As part of our business strategy, we have acquired certain assets of other companies which have had and are expected to continue to have an impact on our results of operations.

In July 2002, through Cypress Communications, we acquired certain assets of Intermedia Advanced Building Networks, the shared tenant telecommunications services business of WorldCom, Inc ( ABN/STS ). The acquisition of

ABN/STS has allowed us to extend our telecommunication services operations to over 5,700 small and medium sized business customers in 25 major metropolitan U.S. markets.

## **Table of Contents**

In March 2003, Cypress Holding, through Cypress Communications, acquired the Southern California building-centric voice and data services business of Eureka Broadband Corporation ( Eureka ). These assets included customer contracts, as well as Eureka s in-building networks and associated building access rights. The acquisition of the Eureka assets has allowed Cypress Holding to expand its telecommunications services operations to include over 750 small and medium sized business customers in the California market.

In July 2003, Cypress Holding, through Cypress Communications, negotiated the surrender of certain assets from E-Building Solutions, Inc. ( E-Building ) in California, a building-centric data services business, to mitigate the loss resulting from E-Building s default on a \$450 note receivable due to Cypress Communications. These assets included customer contracts, as well as E-Building s in-building networks and associated building access rights.

## **Recent Developments**

During the quarter ended September 30, 2004, management determined that we had made payments to telecommunication service providers for federal, state and local taxes and surcharges on telecommunications services for which we might be exempt. We have quantified the amount of taxes we believe were erroneously billed and paid, and are attempting to recover these taxes and surcharges directly from the telecommunications service providers involved. Although management believes that the amount of taxes and surcharges which we are entitled to recover is in the range of \$1,000 to \$2,500, there is no assurance that any amounts will be recovered or when any amounts will be recovered, if ever. The recovery of these taxes and surcharges will be recorded in the financial statements when the taxes and surcharges are actually recovered.

On November 5, 2004, we entered into an Agreement and Plan of Merger (the Merger Agreement ) with TechInvest Holding Company, Inc., an affiliate of Arcapita, Inc. ( Parent ), and TechInvest Acquisition, Inc., a wholly-owned subsidiary of Parent ( Purchaser ), pursuant to which Parent will acquire our company by the merger of Purchaser with and into us, with our company surviving the merger as a wholly-owned subsidiary of Parent. The total value of the transaction, at the time of the execution of the Merger Agreement, was \$39,350. The Merger Agreement contains provisions for final merger consideration adjustments, upwards or downwards, based on the achievement of certain conditions pertaining to changes in certain current assets and liabilities between the execution of the Merger Agreement and closing of the transaction.

On February 3, 2005, in recognition of the potential increase in working capital relating to the telecommunications tax recovery, we agreed with Parent to amend the Merger Agreement (the Amendment ) to increase the merger consideration by \$935, making the total value of the transaction \$40,285. The parties also agreed in the Amendment, among other things, that accounts receivable attributable to the telecommunications tax recovery will be capped in light of the increase in the merger consideration for purposes of calculating the final merger consideration adjustment.

The Merger Agreement provides that the merger consideration will first be used to repay outstanding indebtedness. The remaining consideration, after transaction expenses, will be distributed to stockholders, with an estimated price per share of \$1.71, subject to final merger consideration adjustments (The \$1.71 per share cash consideration is estimated by us as of December 31, 2004 and is subject to adjustment upwards or downwards pursuant to the Merger Agreement).

The closing of the transaction is subject to certain terms and conditions customary for transactions of this type, including receipt of stockholder and regulatory approvals and other conditions.

We incurred \$597 in expenses during 2004 related to the solicitation, negotiation and completion of the sale transaction, which are recorded in general and administrative expense in the consolidated statement of operations.





**Table of Contents****Results of Operations****CYPRESS COMMUNICATIONS HOLDING CO., INC. YEAR ENDED DECEMBER 31, 2004 COMPARED TO YEAR ENDED DECEMBER 31, 2003**

The following table sets forth consolidated financial and operating data as well as the percentage of total revenues represented by certain items in our Consolidated Statements of Operations for the periods indicated:

|                                                 | <b>For the year ended December 31,</b> |                         |             |                         |
|-------------------------------------------------|----------------------------------------|-------------------------|-------------|-------------------------|
|                                                 | <b>2004</b>                            | <b>% of<br/>Revenue</b> | <b>2003</b> | <b>% of<br/>Revenue</b> |
| <b>REVENUES</b>                                 | \$ 78,982                              | 100%                    | \$ 84,626   | 100%                    |
| <b>DIRECT COSTS</b>                             | 37,927                                 | 48%                     | 44,447      | 53%                     |
| <b>REVENUES NET OF DIRECT COSTS</b>             | 41,055                                 | 52%                     | 40,179      | 47%                     |
| <b>OPERATING EXPENSES</b>                       |                                        |                         |             |                         |
| Sales and marketing                             | 2,869                                  | 4%                      | 5,342       | 6%                      |
| General and administrative                      | 35,561                                 | 45%                     | 37,694      | 45%                     |
| Stock based compensation                        | 78                                     |                         | 438         | 1%                      |
| Extinguishment of liabilities and other credits | (545)                                  | (1)%                    | (1,995)     | (2)%                    |
| <b>TOTAL OPERATING EXPENSES</b>                 | 37,963                                 | 48%                     | 41,479      | 49%                     |
| <b>TOTAL OTHER INCOME / (EXPENSE)</b>           | (2,669)                                | (3)%                    | (2,863)     | (3)%                    |
| <b>NET INCOME (LOSS)</b>                        | \$ 423                                 | 1%                      | \$ (4,163)  | (5)%                    |

**REVENUES.** For the year ended December 31, 2004, revenues from our telecommunications services business represented substantially all of our consolidated revenues. Revenues from this business decreased to \$78,982 for the year ended December 31, 2004 from \$84,626 for the year ended December 31, 2003. The decrease in revenues was the result of several factors which began in late 2002 and into 2003 as outlined below:

1. Over the period following the acquisition of the customer base from ABN/STS in mid 2002, there was attrition in this customer base. This was attributable, in part, to the fact that a number of the acquired ABN/STS customers did not fit our overall business model, and terminated their service at the end of the term of their agreements. This customer attrition resulted in the loss of several significant revenue generating customers during 2002 and 2003. The 2004 results reflect the full year impact of this lost revenue.

Management believes that the impact of this post acquisition customer attrition has been substantially realized, and that the future revenue trends will be reflective of more normal customer acquisition and attrition patterns.

2. There was a negative trend in occupancy rates in the commercial real estate business. Occupancy in the types of buildings in which we offer our services declined significantly in the period after 2001. By some industry estimates, vacancy rates in these types of buildings were as high as 30% in some markets. Vacancy rates in buildings we service have a direct impact on our opportunity to add new customers and to retain existing customers.

Based on discussions with building owners and overall industry reports, it appears that occupancy rates began to stabilize during 2004 in the markets where we offer our service. However, the improvement in occupancy rates during 2004 could not offset the full year impact of increased vacancies during 2002 and 2003. Due to the monthly recurring nature of our business and the



**Table of Contents**

relatively small average monthly revenue per customer, our revenue recovery will lag the improvement in the overall trends in occupancy in the buildings we service.

3. The average revenue per customer declined by approximately 3% during the period as a result of the reduction in the average size of our customers combined with pricing reductions related to contract renewals in a large portion of our customer base at rates lower than in previous contracts.

Management believes that the rate of decline in revenues has stabilized, and that projected improvements in real estate occupancy rates in 2005, combined with stabilized employment in the general U.S. economy and the introduction of our EZ Office IP Communications offering should have a positive impact on revenue results going forward.

REVENUES-NET. Revenues-net (after direct costs) increased to approximately \$41,055 for the year ended December 31, 2004 from approximately \$40,179 for the year ended December 31, 2003. Margins increased to approximately 52.0% of revenues in 2004 from approximately 47.5% in 2003, primarily due to reduced network and real estate access related costs as a percentage of revenue.

Management believes that further improvements in margins can be achieved in the future as a result of the efforts expended to date relative to overall reduction in the cost of telecommunications network elements.

OPERATING EXPENSES. Operating expenses decreased to approximately \$37,963 for the year ended December 31, 2004 from approximately \$41,479 for the year ended December 31, 2003. The decrease in operating expenses is primarily due to cost and headcount reduction initiatives implemented starting in late 2002 and into 2003. Included in operating expenses for 2004 is \$597 of costs for investment banking and other costs related to the pending sale of the Company, as described above. Operating expenses decreased as a percentage of revenues to approximately 48% for the year ended December 31, 2004 from approximately 49% for the year ended December 31, 2003 as a result of operating efficiencies achieved through focused cost reduction efforts in all areas of our business. Sales and marketing expenses decreased to \$2,869 for the year ended December 31, 2004 from \$5,342 for the year ended December 31, 2003 due to reductions in the level of bad debt expense in 2004 as compared to 2003, and changes made to the makeup and compensation levels of our sales organization initiated in early 2004. Sales and marketing expense declined as a percentage of revenue to 4% for the year ended December 31, 2004 from approximately 6% for the year ended December 31, 2003 for the reasons noted above. General and administrative expenses decreased to \$35,561 for the year ended December 31, 2004 from \$37,694 for the year ended December 31, 2003 primarily due to the full year impact of cost and headcount reduction measures implemented during 2003. General and administrative expenses as a percentage of revenues was approximately 45% for both years ended December 31, 2004 and 2003. General and administrative expenses for the year ended December 31, 2004 included depreciation and amortization expense of \$774 and expenses in connection with the evaluation, negotiation and closing of the pending sale of the Company of \$597 as mentioned above. Depreciation and amortization expense included in general and administrative expenses for the year ended December 31, 2003 was \$712.

EXTINGUISHMENT OF LIABILITIES AND OTHER CREDITS. The extinguishment of liabilities and other credits for the year ended December 31, 2004 reflects credits of \$545 from settlement and extinguishment of certain liabilities assumed through our acquisition of Cypress Communications. For the year ended December 31, 2003 the extinguishment of liabilities and other credits totaled \$1,995 and was comprised of credits of \$1,019 resulting from negotiated settlements of certain liabilities assumed through our acquisition of Cypress Communications, the recovery of certain assets, originally valued at \$0 for approximately \$378, also acquired through our acquisition of Cypress Communications and the reversal of a previously recorded charge for approximately \$598 resulting from the reactivation of an office facility that had been previously shut-down by our predecessor.

OTHER INCOME AND (EXPENSE). Other income and (expense) was (\$2,669) for the year ended December 31, 2004 as compared with (\$2,863) during year ended December 31, 2003. Interest expense and financing costs were (\$3,022) and (\$2,684) for the years ended December 31, 2004 and 2003

**Table of Contents**

respectively, and consisted primarily of interest expense on debt incurred in 2002 and used in connection with the acquisition of certain assets of ABN/STS, and interest expense incurred on our revolving credit facility.

**INCOME TAXES.** For the years ended December 31, 2004 and 2003, no income tax benefit from our consolidated net operating losses was recognized because of uncertainty as to whether the benefit from such net operating losses will be realized.

**NET INCOME (LOSS).** Our net income for the year ended December 31, 2004 was \$423. For the year ended December 31, 2003, we reported a net loss of \$4,163. The improvement in net income is a direct result of the full year benefit of the cost reductions realized in both our telecommunications and real estate network cost structures, along with reductions in total operating expenses, which exceeded the net decrease in revenues realized.

**CYPRESS COMMUNICATIONS HOLDING CO., INC. YEAR ENDED DECEMBER 31, 2003 COMPARED TO YEAR ENDED DECEMBER 31, 2002**

The following table sets forth consolidated financial and operating data as well as the percentage of total revenues represented by certain items in our Consolidated Statements of Operations for the periods indicated:

|                                                 | <b>For the year ended December 31,</b> |                         |             |                         |
|-------------------------------------------------|----------------------------------------|-------------------------|-------------|-------------------------|
|                                                 | <b>2003</b>                            | <b>% of<br/>Revenue</b> | <b>2002</b> | <b>% of<br/>Revenue</b> |
| <b>REVENUES</b>                                 | \$ 84,626                              | 100%                    | \$ 51,717   | 100%                    |
| <b>DIRECT COSTS</b>                             | 44,447                                 | 53%                     | 28,704      | 56%                     |
| <b>REVENUES NET OF DIRECT COSTS</b>             | 40,179                                 | 47%                     | 23,013      | 44%                     |
| <b>OPERATING EXPENSES</b>                       |                                        |                         |             |                         |
| Sales and marketing                             | 5,342                                  | 6%                      | 3,977       | 8%                      |
| General and administrative                      | 37,694                                 | 45%                     | 25,789      | 50%                     |
| Stock based compensation                        | 438                                    | 1%                      |             |                         |
| Extinguishment of liabilities and other credits | (1,995)                                | (2)%                    |             |                         |
| <b>TOTAL OPERATING EXPENSES</b>                 | 41,479                                 | 49%                     | 29,766      | 58%                     |
| <b>TOTAL OTHER INCOME / (EXPENSE)</b>           | (2,863)                                | (3)%                    | (4,791)     | (9)%                    |
| <b>LOSS FROM CONTINUING OPERATIONS</b>          | (4,163)                                | (5)%                    | (11,544)    | (22)%                   |
| <b>DISCONTINUED OPERATIONS</b>                  |                                        | 0%                      | 2,032       | 4%                      |
| <b>LOSS BEFORE EXTRAORDINARY ITEM</b>           | (4,163)                                | (5)%                    | (9,512)     | (19)%                   |
| <b>EXTRAORDINARY ITEM</b>                       |                                        | 0%                      | 7,783       | 15%                     |
| <b>NET LOSS</b>                                 | \$ (4,163)                             | (5)%                    | \$ (1,729)  | (3)%                    |

**REVENUES.** For the year ended December 31, 2003, revenues from our telecommunications services business represented substantially all of our consolidated revenues. Revenues from this business increased to approximately \$84,626 for the year ended December 31, 2003 from \$51,717 for the year ended December 31, 2002. The increase in revenues resulted from the full year of operations related to the customer base we acquired in July 2002 from ABN/STS, as well as the acquisitions during 2003 of the Eureka and E-Building customer base.

## **Table of Contents**

While overall revenues increased for the year ended December 31, 2003, as indicated above, our quarterly revenues provided a downward trend. This trend was the result of several factors:

1. Over the period following the acquisition of the customer base from ABN/STS, there was attrition in this customer base. This was attributable, in part, to the fact that a number of the acquired ABN/STS customers did not fit our overall business model, and terminated their service at the end of the term of their agreements.
2. There was a negative trend in occupancy rates in the commercial real estate business. Occupancy in the types of buildings in which we offer our services declined significantly in the period after 2001. By some industry estimates, vacancy rates in these type buildings was as high as 30% in some markets. Vacancy rates in buildings we service has a direct impact on our opportunity to add new customers and to retain existing customers.
3. The average revenue per customer declined during the period primarily as a result in reductions in the overall employment within our customer base. As employment falls within our customer base, the average number of users for which we can bill our services declines.

**REVENUES-NET.** Revenues-net (after direct costs) increased to \$40,179 for the year ended December 31, 2003 from \$23,013 for the year ended December 31, 2002. Margins increased to approximately 47.5% of revenues in 2003 from approximately 44.5% in 2002, due to the increased revenue volumes acquired since July 2002, and reduced network costs as a percentage of revenue. Additionally, revenue from the customer bases acquired from Eureka and E-Buildings were substantially for internet services, which results in a lower average margin than our overall business.

**OPERATING EXPENSES.** Operating expenses increased to \$41,479 for the year ended December 31, 2003 from \$29,766 for the year ended December 31, 2002. The increase in operating expenses is primarily due to the full year of operations in 2003 of the ABN/STS business acquired in July 2002, along with additional operating expenses related to the 2003 acquisitions of assets from Eureka and E-Building. Operating expenses decreased as a percentage of revenues to approximately 49% for the year ended December 31, 2003 from approximately 58% for the year ended December 31, 2002 as a result of operating efficiencies achieved through focused cost reduction efforts in all areas of our business. Sales and marketing expenses increased to \$5,342 for the year ended December 31, 2003 from \$3,977 for the year ended December 31, 2002 primarily due to the full year employment in 2003 of sales and marketing personnel we hired during 2002. Sales and marketing expense declined as a percentage of revenue to 6% for the year ended December 31, 2003 from approximately 8% for the year ended December 31, 2002 as a result of restructuring of the sales and marketing functions during 2003 and the efficiencies achieved. General and administrative expenses increased to \$37,694 for the year ended December 31, 2003 from approximately \$25,789 for the year ended December 31, 2002 primarily due to the full year operation of the ABN/STS business acquired in 2002. General and administrative expenses decreased as a percentage of revenues to approximately 45% for the year ended December 31, 2003 from approximately 50% for the year ended December 31, 2002 as a result of efficiencies achieved through the acquisition consolidation. General and administrative expenses for the year ended December 31, 2003 included depreciation and amortization expense of approximately \$712. Depreciation and amortization expense included in general and administrative expenses for the year ended December 31, 2002 was approximately \$146.

**EXTINGUISHMENT OF LIABILITIES AND OTHER CREDITS.** The extinguishment of liabilities and other charges for the year ended December 31, 2003 reflects credits for \$1,019 resulting from negotiated settlements of certain liabilities assumed through our acquisition of Cypress Communications, and the recovery of certain assets, originally valued at \$0 for approximately \$378, also acquired through our acquisition of Cypress Communications and the reversal of a previously recorded charge for approximately \$598 resulting from the reactivation of an office facility that had been previously shut-down.

**OTHER INCOME AND (EXPENSE).** Other income and (expense) was (\$2,863) for the year ended December 31, 2003 as compared with (\$4,791) during year ended December 31, 2002. Interest expense for the year ended

December 31, 2003 was (\$2,684) and consisted primarily of interest expense on



## **Table of Contents**

debt incurred in 2002 and used in connection with acquisition of certain assets of ABN/STS. Interest expense for the year ended December 31, 2002 was (\$4,914) and consisted primarily of interest and finance charges incurred by Cypress Holding in connection with the acquisition of Cypress Communications in February 2002, and the acquisition of certain assets of ABN/STS in July 2002.

**DISCONTINUED OPERATIONS.** There was no income or loss from discontinued operations for the year ended December 31, 2003. Net results from our Latin American operations are included under loss from discontinued operations for the year ended December 31, 2002. Income from discontinued operations was \$2,032 for the year ended December 31, 2002. The income resulted from the recognition of currency exchange gains due to the devaluation of the Argentinean peso after the Argentinean currency crashed in January 2002 and the liquidation of our Latin-American operations in March 2002.

**EXTRAORDINARY GAIN.** The year ended December 31, 2002 includes an extraordinary gain of \$7,783 which resulted from the elimination of all of our long-term assets in an aggregate amount of \$26,840 (Note 4 to Consolidated Financial Statements).

**INCOME TAXES.** For the years ended December 31, 2003 and 2002, no income tax benefit from our consolidated net operating losses was recognized because of uncertainty as to whether the benefit from such net operating losses will be realized.

**NET LOSS.** Our net loss for the year ended December 31, 2003 was \$4,163. For the year ended December 31, 2002, the net loss was \$1,729. The increase in net loss is a direct result of the extraordinary gain of \$7,783 million and income from discontinued operations of \$2,032, both realized in 2002. Without the benefit of the aforementioned gains, the net loss for the year ended December 31, 2002 would have been \$11,544. The network cost reductions and other cost control initiatives implemented during 2002 and 2003 combined with the full year operation of ABN/STS business acquired in 2002, resulted in a significant reduction in the operating loss from continuing operations in 2003 as compared to 2002.

## **Liquidity and Capital Resources**

Beginning in the first quarter of 2002 and continuing throughout 2003 and into early 2004, we initiated certain actions intended to improve liquidity and operating results. Such actions included, among other things, (i) completing the acquisition of Cypress Communications and making certain adjustments to Cypress Communications staffing levels and cost structure, (ii) liquidation of the operations in Argentina and Brazil, (iii) completing the purchase of certain assets of ABN/STS, (iv) raising \$28 million in connection with such asset acquisition and (v) implementing an analysis and optimization project of our telecommunications network and real estate access costs which have resulted in substantial reductions in these cost elements in both absolute terms and as a percentage of revenue.

Our primary sources of liquidity have been proceeds from the issuance of our common stock, convertible debentures, lines of credit and bridge loans, as well as proceeds from the sale of our former North American telecommunications rights operations in December 2000 and cash acquired through our acquisition of Cypress Communications in February 2002.

**Table of Contents**

The following table shows information about our cash flows and liquidity positions as of and for the fiscal years ended December 31, 2004 and 2003. You should read this table and the discussion that follows in conjunction with our consolidated statements of cash flows contained in Item 8 of this report.

|                                                     | <b>Year ended December<br/>31,</b> |             |
|-----------------------------------------------------|------------------------------------|-------------|
|                                                     | <b>2004</b>                        | <b>2003</b> |
| Net cash provided by (used in) operating activities | \$ 1,410                           | \$ (1,397)  |
| Net cash used in investing activities               | (3,622)                            | (5,257)     |
| Net cash provided by financing activities           | 527                                | 296         |
| Net change in cash and cash equivalents             | \$ (1,685)                         | \$ (6,358)  |

For the year ended December 31, 2004, the increase in cash provided by operating activities is primarily attributable to the fact that we recorded net income in 2004 versus a net loss in 2003. The decrease in net cash used in investing activities is reflective of the fact that we acquired business assets of both Eureka and E-Building during 2003, and had no comparable acquisition activity during 2004 outside of capital expenditures to support our current business. Net cash provided by financing activities increased slightly in 2004 as we financed some of our capital expenditures with debt borrowings.

Management believes that our cash position should stabilize during the following quarters as actions initiated starting in 2002 and continuing through early 2004 to reduce our costs have resulted in profitability which we believe is sustainable in the near term. We cannot, however, give any assurance that we will be able to generate sufficient cash flows from operations or financing activities to cover our future costs of operations or to operate on a profitable basis. Likewise, no assurance can be given that we can generate sufficient cash flow from operations or financing activities to support our debt service obligations, including debt raised in connection with our acquisition of certain assets from ABN/STS. Moreover, the terms of the indebtedness we incurred in connection with the acquisition of certain assets from ABN/STS contain restrictive covenants that limit our ability to incur additional indebtedness, pay dividends or undertake certain other transactions. We have also pledged certain assets as security under our Senior Credit Facility. Therefore, we must devote a substantial portion of our cash flow to service our indebtedness and cannot utilize that cash flow for operations. Accordingly, there can be no assurance that we will have sufficient liquidity to implement our business plan. Likewise, there can also be no assurance that we will be able to obtain cash through future financing activities on acceptable terms, or at all, or that we will ever become profitable.

As noted in the accompanying financial statements, we have Bridge Loan debt and fees totaling \$8,480 which will come due in July 2005. At present, we have not initiated a process to refinance this debt, pending the proposed acquisition of the Company as discussed elsewhere in this report. Should that acquisition fail to be completed as currently contemplated, we would be required to either renegotiate the terms of the Bridge Loan with the current debt holders, or seek replacement financing. Our inability to renegotiate the terms of the Bridge Loan, or find replacement financing would have a serious negative financial impact on the Company's liquidity and ability to finance its operations.

As of December 31, 2004, we had cash and cash equivalents of \$215 as compared to \$1,900 at December 31, 2003. In addition, at December 31, 2004 we had approximately \$5,000 of borrowing availability under the terms of our senior credit facility. Management attempts to balance cash balances on-hand, and anticipated cash needs with the availability under the Senior Credit Facility so as to minimize interest and finance charges incurred. Our business has

some seasonality primarily attributable to usage charges for voice services, which generally decline during holiday periods such as Thanksgiving, Christmas and New Years and during the summer months; however, the effects of such seasonality have not had, and are not expected to have, a material impact on our liquidity. Assuming that we are able to either renegotiate the terms of the Bridge Loan, or find replacement financing, cash generated from operations,

**Table of Contents**

along with the availability under our line of credit, is expected to be sufficient to fund our operations for at least the next twelve months.

**Contractual Obligations and Commitments**

The following table contains information relating to our contractual obligations and commitments for the five years subsequent to December 31, 2004 and thereafter. The amounts represent the maximum future contractual obligations and are reported without giving effect to any related discounts, premiums and other adjustments necessary to comply with accounting principles generally accepted in the U.S. In addition, we have an unused line of credit outstanding totaling approximately \$7,400 at December 31, 2004 subject to certain borrowing base limitations.

|                                                     |           | Payments Due by Period |              |              |              |
|-----------------------------------------------------|-----------|------------------------|--------------|--------------|--------------|
|                                                     |           | Less<br>than           | 1-3<br>Years | 3-5<br>Years | More<br>than |
|                                                     | Total     | 1 Year                 |              |              | 5 Years      |
| Long-Term Debt Obligations                          | 20,576    | 10,576 (1)             |              | 10,000 (2)   |              |
| Interest Expense on Debt                            | 7,910     | 1,087                  |              | 6,823        |              |
| Capital Leases                                      | 35        | 31                     | 4            |              |              |
| Operating Leases                                    | 11,457    | 4,718                  | 5,185        | 1,392        | 162          |
| Obligations under license agreements                | 4,492     | 1,120                  | 1,767        | 1,110        | 495          |
| Obligations under communications service agreements | 10,449    | 10,311                 | 138          |              |              |
| Total contractual cash obligations                  | \$ 54,919 | \$ 27,843              | \$ 7,094     | \$ 19,325    | \$ 657       |

(1) Includes \$8,000 due under the Bridge Loan, which accrues interest at 14% per annum, and matures on the earlier to occur of (i) one business day following the maturity of the Senior Credit Facility, (ii) July 16, 2005 and (iii) an event whereby we substantially refinance our debt obligations, and \$2,576 due under the Senior Credit Facility, which currently has a maturity of July 11, 2005. We expect to renew the Senior Credit Facility on similar terms upon its maturity, but there is no assurance that we will be able to do so.

(2) The Convertible Notes accrue interest at the rate of 7.5% per annum, compounded quarterly, and payable at maturity of the notes, whether upon their stated maturity of July 1, 2009, or earlier as a result of acceleration in the event of a default or upon redemption of the Convertible Notes. The principal of and accrued interest on the Convertible Notes is convertible into our common stock at \$1.13 per share. The Convertible Notes are redeemable by us at any time by payment of the outstanding principal balance and accrued interest. In the event that the Convertible Notes are redeemed, the Purchasers have been issued warrants which will then be eligible for exercise to purchase the number of shares of our common stock that the Convertible Notes were convertible into on the redemption date at a conversion price of \$1.13 per share.

**Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures, or capital resources that are material to investors.

**Critical Accounting Policies**

Management's Discussion and Analysis of Financial Condition and Results of Operations are based upon our Consolidated Financial Statements and the notes thereto, which have been prepared in accordance with generally accepted accounting principles. We are required to make, in the preparation of

## **Table of Contents**

the Consolidated Financial Statements, estimates and judgments that affect the reported amounts of assets, liabilities, revenue, and expenses, and related disclosure of contingent assets and liabilities. We have reviewed the accounting policies used in reporting our financial results on a regular basis. Management has reviewed the accounting policies and related disclosures with our Audit Committee.

The following is not intended to be a comprehensive list of all of our accounting policies. Our significant accounting policies are more fully described in Note 1 to the Consolidated Financial Statements. In many cases, the accounting treatment of a particular transaction is specifically dictated by accounting principles generally accepted in the United States of America, with no need for management's judgment in their application. There are also areas in which management's judgment in selecting an available alternative would not produce a materially different result.

We have identified the following as accounting policies critical to us:

### **ACCOUNTING ESTIMATES**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect that reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### **CASH AND CASH EQUIVALENTS**

Cash equivalents consist of short-term, highly liquid investments that mature in three months or less, which are readily convertible into cash.

### **PROPERTY, EQUIPMENT AND DEPRECIATION**

Property and equipment are stated at cost. Depreciation is computed over the estimated useful lives of the assets (three to seven years) by straight-line methods for financial reporting purposes. Depreciation of leasehold improvements is computed over the lesser of the estimated useful lives of the assets or the term of the lease by the straight-line method for financial reporting purposes.

### **REVENUE RECOGNITION**

The Company's revenues include recurring charges for local access, long-distance, equipment rental, Internet access, digital satellite business television, voicemail, inbound 800, and other enhanced voice and data services, which are recognized as services provided. Revenues also include nonrecurring charges for installations and moves, adds, and changes. Installation fees represent the initial cost charged by Cypress Communications for installing voice phone lines, data lines, and business class cable television in the tenant's premises. Move, add, and change (MAC) charges are for the Company's labor and materials related to moving, adding, or changing a customer's services. Installation and MAC charges are recognized when the services are provided as they represent a separate earnings process. Revenues are net of certain credits and discounts. Deferred revenue represents monthly recurring charges received in advance.

### **STOCK-BASED COMPENSATION**

The Company follows The Financial Accounting Standards Board Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation* (SFAS No. 123), amended by SFAS No. 148, *Accounting for Stock Based compensation Transition and Disclosure*. SFAS No. 123 encourages companies to recognize expense for stock options and other stock-based employee compensation plans based on their fair value at the date of grant. As

permitted by SFAS No. 123, the Company has and will retain its prior accounting policy under APB Opinion Number 25, Accounting for Stock Issued to Employees, and, accordingly, compensation expense for stock options is measured as the excess, if any, of the fair value of the Company's stock at the date of grant over the exercise price.

FASB Statement 123, Accounting for Stock Based Compensation, requires the Company to provide pro forma information regarding net income and earnings per share as if compensation cost for the Company's stock option plan has been determined in accordance with the fair value based method prescribed in FASB Statement 123. The Company estimates the fair value of each stock option at the grant date by using the Black-Scholes option-pricing model with the following assumptions used for grants in both 2004, 2003 and 2002: no dividends yield for all years; expected volatility of 100%, 100% and 74%, respectively; risk-free interest rate of 4.26%, 3.0% and 4.42%, respectively and expected life of 7 years for all periods.

#### FAIR VALUES OF FINANCIAL INSTRUMENTS

The Company's financial instruments consist principally of cash and cash equivalents, accounts receivable, accounts payable, accrued liabilities and notes. The carrying amounts of such financial instruments as reflected in the balance sheet approximate their estimated fair value as of December 31, 2004 and 2003 due to their short-term nature. The estimated fair value is not necessarily indicative of the amounts the Company could realize in a current market exchange or of future earnings or cash flows.

#### VALUATION OF LONG-LIVED ASSETS

On January 1, 2002, the Company adopted FASB Statement No. 144 Accounting for Impairment or Disposal of Long-Lived Assets (FAS No. 144). Under FAS 144, the Company reviews long-lived assets for impairment when circumstances indicate the carrying amount of an asset may not be recoverable based on the undiscounted future cash flows of the asset. If the carrying amount of the asset is determined not to be recoverable, a write-down to fair value is recorded.

#### INCOME TAXES

Income taxes are accounted for under FASB Statement No. 109, Accounting for Income Taxes (FAS 109). FAS 109 is an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in our financial statements or tax returns. In estimating future tax consequences, FAS 109 generally considers all expected future events other than proposed changes in the tax laws or rates. Valuation allowances are provided if it is more likely than not that a deferred tax asset will not be realized.

#### NET INCOME (LOSS) PER COMMON SHARE BASIC AND DILUTED

Basic earnings per share (EPS) is calculated by dividing the income (loss) available to common shareholders by the weighted average number of common shares outstanding for the period, without consideration for common stock equivalents. Diluted EPS gives effect to all dilutive potential common shares outstanding for the period. Shares of common stock issuable upon the exercise of options (3,462, 3,897 and 3,770 shares in 2004, 2003 and 2002, respectively) and warrants (1,742, 2,346 and 3,143 shares

## **Table of Contents**

in 2004, 2003 and 2002, respectively) and shares issued upon conversion of convertible notes (10,619, 9,859 and 9,153 in 2004, 2003 and 2002, respectively) are antidilutive and are not included in the computation of shares outstanding.

### **COMPREHENSIVE INCOME (LOSS)**

The Company follows SFAS No. 130, Reporting Comprehensive Income ( SFAS 130 ). SFAS 130 establishes standards for reporting comprehensive income or loss and its components in the consolidated financial statements. Comprehensive income (loss), as defined, includes all changes in equity (net assets) during a period from non-owner sources. To date, the Company has reported other comprehensive income from the cumulative effect on exchange rates for the amount of \$0 in 2004, \$0 in 2003 and \$(2,170) in 2002. The Company had no other material transactions that are required to be reported in comprehensive income or loss.

### **SEGMENT REPORTING**

The Company operates in one business segment the provision of telecommunication services to small and medium sized businesses on an integrated basis.

### **RECENT ACCOUNTING PRONOUNCEMENTS**

On December 16, 2004, the FASB issued Statement 123 (revised 2004) that will require compensation costs related to share-based payment transactions to be recognized in the financial statements. With limited exceptions, the amount of compensation cost will be measured based on the grant-date fair value of the equity or liability instruments issued. In addition, liability awards will be re measured each reporting period. Compensation cost will be recognized over the period that an employee provides service in exchange for the award. Statement 123(R) replaces FASB Statement No. 123, Accounting for Stock-Based Compensation, and supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees. The effective date for this requirement is as of the first interim or annual reporting period that begins after June 15, 2005. The company has not estimated the impact of adopting this revised standard on the financial statements.

In November 2004, the FASB issued SFAS No. 151, Inventory Costs an amendment of ARB No. 43, Chapter 4. SFAS No. 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs and wasted materials (or spoilage) should be recognized as current-period charges and requires the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. SFAS No. 151 is effective for fiscal years beginning after June 15, 2005. It is not expected that the adoption of SFAS No. 151 to have any effect on the Company's consolidated financial position or results of operations.

In December 2003, the FASB issued a revision to FASB Interpretation No. 46, Consolidation of Variable Interest Entities (FIN 46-R). FIN 46 is an Interpretation of Accounting Research Bulletin 51, Consolidated Financial Statements and addresses consolidation by business enterprises of variable interest entities (VIEs) that possess certain characteristics. The revision clarifies the definition in the original release that potentially could have classified any business as a VIE. The revision also delays the effective date of the Interpretation from the first reporting following December 15, 2003 to the first reporting period ending after March 15, 2004. The revision was effective for the Company in the first quarter of fiscal 2004. No VIEs have been identified and, accordingly, the application of the Interpretation did not have an effect on the Company's results of operations or financial position.

### **ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**



We are exposed to interest rate changes, primarily as a result any borrowing under our line of credit facility which has a variable interest rate equal to the prime rate, as announced from time to time by Silicon Valley Bank, plus 2.0%. No action has been taken to cover our interest rate market risk, and we are not a party to any interest rate market risk management activities.

Our long term debt at December 31, 2004, carries interest rates, which are fixed. Our line of credit pursuant to our senior credit facility with Silicon Valley Bank carries interest rates, which vary with the prime rate. Accordingly, any increases in the prime rate will reduce our earnings. A 1% increase in the prime rate on the \$2,576 million outstanding under our line of credit at December 31, 2004 would result in an annual interest expense increase of \$26.

**Table of Contents**

**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

**TABLE**

|                                                                                                                                  |    |
|----------------------------------------------------------------------------------------------------------------------------------|----|
| CYPRESS COMMUNICATIONS HOLDING CO., INC.                                                                                         |    |
| <u>Report of Independent Registered Public Accounting Firm</u>                                                                   | 35 |
| <u>Consolidated Balance Sheet as of December 31, 2004 and 2003</u>                                                               | 36 |
| <u>Consolidated Statements of Operations for the year ended December 31, 2004, 2003 and 2002</u>                                 | 37 |
| <u>Consolidated Statements of Changes In Stockholders' Equity (Deficit) for the years ended December 31, 2004, 2003 and 2002</u> | 38 |
| <u>Consolidated Statements of Cash Flows for the years ended December 31, 2004, 2003 and 2002</u>                                | 40 |
| <u>Notes to Consolidated Financial Statements</u>                                                                                | 42 |
| CYPRESS COMMUNICATIONS, INC. (Predecessor)                                                                                       | 62 |
| <u>Independent Auditors' Report</u>                                                                                              | 62 |
| <u>Consolidated Statement of Operations for the One-Month Period from January 1, 2002 to January 31, 2002</u>                    | 63 |
| <u>Consolidated Statement of Stockholders' Equity for the One-Month Period from January 1, 2002 to January 31, 2002</u>          | 64 |
| <u>Consolidated Statement of Cash Flows for the One-Month Period from January 1, 2002 to January 31, 2002</u>                    | 65 |
| <u>Notes to Consolidated Financial Statements</u>                                                                                | 66 |

**Table of Contents**

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Stockholders of Cypress Communications Holding Company, Inc.:

We have audited the accompanying consolidated balance sheets of Cypress Communications Holding Company, Inc. and subsidiaries (the Company formerly U.S. RealTel, Inc.) as of December 31, 2004 and 2003 and the related consolidated statements of operations, changes in stockholders' equity (deficit) and cash flows for each of the three years in the period ended December 31, 2004. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 2 to the consolidated financial statements, the Company has suffered recurring losses from operations and is in an unfavorable working capital and uncertain liquidity position that raises substantial doubt about its ability to continue as a going concern. Management's plans concerning these matters are also described in Note 2. The consolidated financial statements do not include any adjustments relating to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Company be unable to continue as a going concern.

/s/ Deloitte & Touche, LLP

Atlanta, GA  
April 15, 2005

Table of Contents

## CYPRESS COMMUNICATIONS HOLDING CO., INC.

## CONSOLIDATED BALANCE SHEET

December 31, 2004 and 2003

(In thousands, except share  
data)

|                                                                                              | 2004             | 2003             |
|----------------------------------------------------------------------------------------------|------------------|------------------|
| <b>ASSETS</b>                                                                                |                  |                  |
| <b>CURRENT ASSETS</b>                                                                        |                  |                  |
| Cash and cash equivalents                                                                    | \$ 215           | \$ 1,900         |
| Accounts receivable, net of allowance for doubtful accounts of \$257 and \$412, respectively | 6,796            | 7,652            |
| Prepaid expenses and other current assets                                                    | 1,208            | 1,271            |
| <b>TOTAL CURRENT ASSETS</b>                                                                  | <b>8,219</b>     | <b>10,823</b>    |
| <b>PROPERTY AND EQUIPMENT, NET (Note 5)</b>                                                  | <b>\$ 23,628</b> | <b>\$ 24,249</b> |
| <b>INTANGIBLE ASSETS, NET</b>                                                                | <b>92</b>        | <b>523</b>       |
|                                                                                              | <b>\$ 31,939</b> | <b>\$ 35,595</b> |
| <b>LIABILITIES AND STOCKHOLDERS' DEFICIT</b>                                                 |                  |                  |
| <b>CURRENT LIABILITIES</b>                                                                   |                  |                  |
| Accounts payable and accrued expenses (Note 7)                                               | \$ 10,268        | \$ 16,344        |
| Line of credit (Note 8)                                                                      | 2,576            | 2,016            |
| Deferred revenue                                                                             | 1,077            | 1,310            |
| Current portion of long term debt (Note 8)                                                   | 8,511            | 494              |
| <b>TOTAL CURRENT LIABILITIES</b>                                                             | <b>22,432</b>    | <b>20,164</b>    |
| <b>Long term debt (Note 8)</b>                                                               | <b>10,463</b>    | <b>17,543</b>    |
| <b>Accrued liabilities, long-term</b>                                                        | <b>970</b>       | <b>315</b>       |
| <b>TOTAL LONG-TERM LIABILITIES</b>                                                           | <b>11,433</b>    | <b>17,858</b>    |
| <b>COMMITMENTS AND CONTINGENCIES (Notes 8 and 9)</b>                                         |                  |                  |
| <b>STOCKHOLDERS' DEFICIT (Note 10)</b>                                                       |                  |                  |
| Preferred stock, \$.001 par value; 5,000,000 shares authorized; (100 Series A issued)        |                  |                  |

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|                                                                                                |             |             |
|------------------------------------------------------------------------------------------------|-------------|-------------|
| Common stock, \$.001 par value; 50,000,000 shares authorized; 6,467,808 issued and outstanding | 6           | 6           |
| Additional paid-in capital                                                                     | 23,685      | 23,607      |
| Accumulated deficit                                                                            | (24,757)    | (25,180)    |
| Less: Treasury Stock, at cost; 594,413 shares (Note 11)                                        | (860)       | (860)       |
| <br>TOTAL STOCKHOLDERS DEFICIT                                                                 | <br>(1,926) | <br>(2,427) |
|                                                                                                | \$ 31,939   | \$ 35,595   |

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Table of Contents**

## CYPRESS COMMUNICATIONS HOLDING CO., INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

Years ended December 31, 2004, 2003 and 2002

|                                                 | (In thousands, except per share data) |            |            |
|-------------------------------------------------|---------------------------------------|------------|------------|
|                                                 | 2004                                  | 2003       | 2002       |
| REVENUES, NET                                   | \$ 78,982                             | \$ 84,626  | \$ 51,717  |
| DIRECT COSTS                                    | 37,927                                | 44,447     | 28,704     |
| REVENUES NET OF DIRECT COSTS                    | 41,055                                | 40,179     | 23,013     |
| OPERATING EXPENSES                              |                                       |            |            |
| Sales and marketing                             | 2,869                                 | 5,342      | 3,977      |
| General and administrative                      | 35,561                                | 37,694     | 25,789     |
| Extinguishment of liabilities and other credits | (545)                                 | (1,995)    |            |
| Stock based compensation                        | 78                                    | 438        |            |
| TOTAL OPERATING EXPENSES                        | 37,963                                | 41,479     | 29,766     |
| OTHER INCOME (EXPENSE)                          |                                       |            |            |
| Interest income                                 |                                       | 17         | 60         |
| Interest expense and financing costs (Notes 8)  | (3,022)                               | (2,684)    | (4,914)    |
| Net gain (loss) on disposal of assets           | 417                                   | 61         | (22)       |
| Gain on extinguishment of debt                  |                                       |            | 85         |
| Net gain (loss) on investment                   |                                       | (149)      |            |
| Other                                           | (64)                                  | (108)      |            |
| TOTAL OTHER INCOME (EXPENSE) NET                | (2,669)                               | (2,863)    | (4,791)    |
| Income (loss) From Continuing Operations        | 423                                   | (4,163)    | (11,544)   |
| GAIN (LOSS) FROM DISCONTINUED OPERATIONS        |                                       |            | 2,032      |
| Income (loss) Before Extraordinary Item         | 423                                   | (4,163)    | (9,512)    |
| Extraordinary Item gain on acquisition (Note 4) |                                       |            | 7,783      |
| Net income (loss) before income taxes           | \$ 423                                | \$ (4,163) | \$ (1,729) |
| Income taxes                                    |                                       |            |            |
| Net income (loss)                               | \$ 423                                | \$ (4,163) | \$ (1,729) |
| Net Income (Loss) Per Common Share              |                                       |            |            |
| Income (loss) from continuing operations        | \$ 0.07                               | \$ (0.71)  | \$ (1.95)  |
| Gain (loss) from discontinued operations        |                                       |            | 0.34       |

|                                                      |         |           |           |      |
|------------------------------------------------------|---------|-----------|-----------|------|
| Extraordinary item                                   |         |           |           | 1.32 |
| Net Income (Loss) Per Common Share Basic and Diluted | \$ 0.07 | \$ (0.71) | \$ (0.29) |      |
| Weighted Average Common Shares Outstanding           | 5,874   | 5,874     | 5,894     |      |

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Table of Contents

## CYPRESS COMMUNICATIONS HOLDING CO., INC.

## CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

(All dollar and share amounts are presented in thousands, except per share amounts)

|                                                  | Preferred<br>Stock<br>Shares | Preferred<br>Stock<br>Amount | Common<br>Stock<br>Shares | Common<br>Stock<br>Amount | Addi-<br>tional<br>Paid-in<br>Capital | Accu-<br>mulated<br>Deficit | Compre-<br>hensive<br>Income<br>(Loss) | Accu-<br>mulated<br>Other<br>Compre-<br>hensive<br>Income | Treasury<br>Stock<br>Shares | Treasury<br>Stock<br>Amount | Total    |
|--------------------------------------------------|------------------------------|------------------------------|---------------------------|---------------------------|---------------------------------------|-----------------------------|----------------------------------------|-----------------------------------------------------------|-----------------------------|-----------------------------|----------|
| Balance, at<br>December 31,<br>2001              |                              |                              | 6,468                     | \$ 6                      | \$ 19,599                             | \$ (19,288)                 |                                        | \$ 2,170                                                  | 533                         | \$ (800)                    | \$ 1,687 |
| Stock Warrants                                   |                              |                              |                           |                           | 1,181                                 |                             |                                        |                                                           |                             |                             | 1,181    |
| Issuance of<br>Preferred Stock                   |                              |                              |                           |                           |                                       |                             |                                        |                                                           |                             |                             |          |
| Beneficial<br>Conversion<br>Feature (Note<br>10) |                              |                              |                           |                           | 2,389,000                             |                             |                                        |                                                           |                             |                             | 2,389    |
| Payment for<br>Treasury Stock<br>(Note 11)       |                              |                              |                           |                           |                                       |                             |                                        |                                                           | 61                          | (60)                        | (60)     |
| Net loss                                         |                              |                              |                           |                           |                                       | (1,729)                     | (1,729)                                |                                                           |                             |                             | (1,729)  |
| Other<br>Comprehensive<br>Loss                   |                              |                              |                           |                           |                                       |                             | (2,170)                                | (2,170)                                                   |                             |                             | (2,170)  |
| Comprehensive<br>Loss                            |                              |                              |                           |                           |                                       |                             | \$ (3,899)                             |                                                           |                             |                             |          |
| Balance, at<br>December 31,<br>2002              |                              |                              | 6,468                     | \$ 6                      | \$ 23,169                             | \$ (21,017)                 | \$                                     | \$                                                        | 594                         | \$ (860)                    | \$ 1,298 |
|                                                  |                              |                              |                           |                           | 438                                   |                             |                                        |                                                           |                             |                             | 438      |



Stock Based  
Compensation

|                       |         |         |         |
|-----------------------|---------|---------|---------|
| Net loss              | (4,163) | (4,163) | (4,163) |
| Comprehensive<br>Loss |         | (4,163) |         |

Balance, at  
December 31,  
2003

|       |    |   |    |        |    |          |    |     |    |       |    |         |
|-------|----|---|----|--------|----|----------|----|-----|----|-------|----|---------|
| 6,468 | \$ | 6 | \$ | 23,607 | \$ | (25,180) | \$ | 594 | \$ | (860) | \$ | (2,427) |
|-------|----|---|----|--------|----|----------|----|-----|----|-------|----|---------|

Stock Based  
Compensation

|    |    |
|----|----|
| 78 | 78 |
|----|----|

38

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**Table of Contents**

|                               | Preferred Stock |        | Common Stock |        | Additional Paid-in Capital | Accumulated Deficit | Comprehensive Income (Loss) | Accumulated Other Comprehensive Income | Treasury Stock | Total               |
|-------------------------------|-----------------|--------|--------------|--------|----------------------------|---------------------|-----------------------------|----------------------------------------|----------------|---------------------|
|                               | Shares          | Amount | Shares       | Amount |                            |                     |                             |                                        | Shares         | Amount              |
| Net Income                    |                 |        |              |        |                            | 423                 | 423                         |                                        |                | 423                 |
| Comprehensive Income          |                 |        |              |        |                            |                     | 423                         |                                        |                |                     |
| Balance, at December 31, 2004 |                 |        | 6,468        | \$ 6   | \$ 23,685                  | \$ (24,757)         |                             | \$                                     | 594            | \$ (860) \$ (1,926) |

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Table of Contents**

## CYPRESS COMMUNICATIONS HOLDING CO., INC.

## CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31, 2004, 2003, and 2002

(In thousands)

|                                                                                     | 2004        | 2003        | 2002         |
|-------------------------------------------------------------------------------------|-------------|-------------|--------------|
| <b>Cash Flows From Operating Activities</b>                                         |             |             |              |
| Net income (loss)                                                                   | \$ 423      | \$ (4,163)  | \$ (1,729)   |
| Adjustments to reconcile net income (loss) to net cash used in operating activities |             |             |              |
| Depreciation and amortization                                                       | 4,932       | 4,246       | 1,459        |
| Bad debt expense                                                                    | 421         | 1,697       | 679          |
| Stock based compensation                                                            | 78          | 438         |              |
| Stock warrants issued in connection with acquisition                                |             |             | 1,181        |
| (Gain) Loss on disposal of assets and extinguishment of debt                        | (779)       | 196         |              |
| Extraordinary gain                                                                  |             |             | (7,783)      |
| Discontinued operations                                                             |             |             | (2,207)      |
| Amortization of warrant cost as interest expense                                    | 475         | 608         | 305          |
| Other non-cash items                                                                |             |             | 85           |
| Changes in assets and liabilities, net of dispositions                              |             |             |              |
| (Increase) decrease in accounts receivable                                          | 1,011       | (517)       | 4,408        |
| (Increase) decrease in prepaid expenses and other current assets                    | 63          | 80          | (956)        |
| (Increase) decrease in other assets                                                 |             | (45)        | (619)        |
| Increase (decrease) in accounts payable and accrued expenses                        | (4,981)     | (4,777)     | 11,117       |
| Increase (decrease) in deferred revenue                                             | (233)       | 840         | (794)        |
| <br>Net cash provided by (used in) operating activities                             | <br>1,410   | <br>(1,397) | <br>5,146    |
| <br><b>Cash Flows From Investing Activities</b>                                     |             |             |              |
| Investment in subsidiary                                                            |             |             | (48,495)     |
| Capital expenditures                                                                | (4,040)     | (1,941)     | (1,050)      |
| Purchase of assets related to Eureka and E-Building acquisitions                    |             | (3,543)     |              |
| Sale of property and equipment                                                      | 418         | 227         |              |
| Cash acquired in acquisitions                                                       |             |             | 33,023       |
| <br>Net cash used in investing activities                                           | <br>(3,622) | <br>(5,257) | <br>(16,522) |
| <br><b>Cash Flows From Financing Activities</b>                                     |             |             |              |
| Proceeds from note payable in connection to acquisition                             |             |             | 16,436       |
| Repayment of note payable in connection with acquisition                            |             |             | (16,436)     |
| Borrowings from credit facilities, net of repayments                                | 560         | 2,016       | 26,551       |

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|                                           |      |         |         |
|-------------------------------------------|------|---------|---------|
| Principal payments of long-term debt      | (33) | (1,720) | (8,918) |
| Payment for acquisition of treasury stock |      |         | (60)    |
| Net cash provided by financing activities | 527  | 296     | 17,573  |

40

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**Table of Contents**

|                                                                            | 2004       | 2003         | 2002         |
|----------------------------------------------------------------------------|------------|--------------|--------------|
| Net Increase (Decrease) in Cash and Cash Equivalents                       | (1,685)    | (6,358)      | 6,197        |
| Cash and Cash Equivalents, at beginning of year                            | 1,900      | 8,258        | 2,061        |
| <br>Cash and Cash Equivalents, at end of year                              | <br>\$ 215 | <br>\$ 1,900 | <br>\$ 8,258 |
| <br>Supplemental Disclosure of Cash Flow Information                       |            |              |              |
| Interest paid                                                              | \$ 1,432   | \$ 1,246     | \$ 4,914     |
| <br>Supplemental Disclosures of Noncash Investing and Financing Activities |            |              |              |
| Warrants issued for financing costs                                        |            |              | 1,181        |

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

**Table of Contents**

## CYPRESS COMMUNICATIONS HOLDING CO., INC.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2004, 2003 and 2002

**(All dollar and share amounts are presented in thousands, except per share amounts)**

## 1. ORGANIZATION, BASIS OF PRESENTATION AND ACCOUNTING POLICIES

## ORGANIZATION

Cypress Communications Holding Co., Inc. (together with its subsidiaries, Cypress Holding or the Company ) (formerly U.S. RealTel, Inc.), through its wholly owned operating subsidiary, Cypress Communications, Inc. ( Cypress Communications or Cypress ) provides comprehensive data, voice and video communications services to small and medium sized businesses located in approximately 1,300 commercial office buildings in select major metropolitan markets within the United States. The Company is incorporated under the laws of the State of Delaware.

In July 2002, through Cypress Communications, we acquired certain assets of Intermedia Advanced Building Networks, the shared tenant telecommunications services business of WorldCom, Inc (ABN/STS). The acquisition of ABN/STS has allowed us to extend our telecommunications services operations to over 5,700 small and medium sized business customers in 25 major metropolitan U.S. markets.

## BASIS OF PRESENTATION

The accompanying financial statements are presented on the accrual basis of accounting using accounting principles generally accepted in the United States.

## PRINCIPLES OF CONSOLIDATION

Cypress Holding's subsidiaries at December 31, 2004 are listed below:

|                                                         | Location    | Percent Owned | Description         |
|---------------------------------------------------------|-------------|---------------|---------------------|
| Cypress Communications, Inc.                            | Atlanta, GA | 100%          | Active subsidiary   |
| Cypress Communications Operating Company, LLC           | Atlanta, GA | 100%          | Active subsidiary   |
| Cypress Communications Holding Company of Virginia, LLC | Atlanta, GA | 100%          | Active subsidiary   |
| Cypress Communications International, Inc.              | Atlanta, GA | 100%          | Inactive subsidiary |

|                     |        |      |                        |
|---------------------|--------|------|------------------------|
| Cypress Canada Inc. | Canada | 100% | Inactive<br>subsidiary |
|---------------------|--------|------|------------------------|

## **Table of Contents**

The consolidated financial statements include the accounts of Cypress Holding and its subsidiaries that are more than 50% owned.

All significant intercompany transactions and balances between the companies included in the consolidation are eliminated.

## **ACCOUNTING ESTIMATES**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect that reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

## **CASH AND CASH EQUIVALENTS**

Cash equivalents consist of short-term, highly liquid investments that mature in three months or less, which are readily convertible into cash.

## **PROPERTY, EQUIPMENT AND DEPRECIATION**

Property and equipment are stated at cost. Depreciation is computed over the estimated useful lives of the assets (three to seven years) by straight-line methods for financial reporting purposes. Depreciation of leasehold improvements is computed over the lesser of the estimated useful lives of the assets or the term of the lease by the straight-line method for financial reporting purposes.

## **REVENUE RECOGNITION**

The Company's revenues include recurring charges for local access, long-distance, equipment rental, Internet access, digital satellite business television, voicemail, inbound 800, and other enhanced voice and data services, which are recognized as services provided. Revenues also include nonrecurring charges for installations and moves, adds, and changes. Installation fees represent the initial cost charged by Cypress Communications for installing voice phone lines, data lines, and business class cable television in the tenant's premises. Move, add, and change (MAC) charges are for the Company's labor and materials related to moving, adding, or changing a customer's services. Installation and MAC charges are recognized when the services are provided as they represent a separate earnings process. Revenues are net of certain credits and discounts.

## **STOCK-BASED COMPENSATION**

The Company follows The Financial Accounting Standards Board Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation* (SFAS No. 123), amended by SFAS No. 148, *Accounting for Stock Based compensation Transition and Disclosure*. SFAS No. 123 encourages companies to recognize expense for stock options and other stock-based employee compensation plans based on their fair value at the date of grant. As permitted by SFAS No. 123, the Company has and will retain its prior accounting policy under APB Opinion Number 25, *Accounting for Stock Issued to Employees*, and, accordingly, compensation expense for stock options is measured as the excess, if any, of the fair value of the Company's stock at the date of grant over the exercise price.

FASB Statement 123, *Accounting for Stock Based Compensation*, requires the Company to provide pro forma information regarding net income and earnings per share as if compensation cost for the Company's stock option plan has been determined in accordance with the fair value based method prescribed in FASB Statement 123. The



Company estimates the fair value of each stock option at the grant date by using the Black-Scholes option-pricing model with the following assumptions used for grants in both 2004, 2003 and 2002: no dividends yield for all years; expected volatility of 100%, 100% and 74%,

**Table of Contents**

respectively; risk-free interest rate of 4.26%, 3.0% and 4.42%, respectively and expected life of 7 years for all periods.

The following table illustrates the effect on the loss and loss per share if Cypress Holding had applied the fair value recognition provisions of SFAS No. 123, *Accounting for Stock-Based Compensation*, to stock-based employee compensation:

|                                                                                                            | <b>Years Ended December 31,</b> |             |             |
|------------------------------------------------------------------------------------------------------------|---------------------------------|-------------|-------------|
|                                                                                                            | <b>2004</b>                     | <b>2003</b> | <b>2002</b> |
| Net income (loss), as reported                                                                             | \$ 423                          | \$ (4,163)  | \$ (1,729)  |
| Add: Stock-based compensation, as reported                                                                 | 78                              | 438         |             |
| Deduct: Total stock based compensation determined under fair value based method for all awards, net of tax | (1,269)                         | (1,141)     | (4,960)     |
| Pro forma net loss                                                                                         | \$ (768)                        | \$ (4,866)  | \$ (2,225)  |
| Income (loss) per share:                                                                                   |                                 |             |             |
| Basic and diluted income (loss) per share as reported                                                      | \$ 0.07                         | \$ (.71)    | \$ (0.29)   |
| Basic and diluted loss per share as pro forma                                                              | \$ (0.13)                       | (.83)       | (0.38)      |

**ADVERTISING COSTS**

Advertising costs, aggregating \$40 in 2004, \$90 in 2003 and \$60 in 2002, are expensed as incurred.

**FAIR VALUES OF FINANCIAL INSTRUMENTS**

The Company's financial instruments consist principally of cash and cash equivalents, accounts receivable, accounts payable, accrued liabilities and notes. The carrying amounts of such financial instruments as reflected in the balance sheet approximate their estimated fair value as of December 31, 2004 and 2003 due to their short-term nature. The estimated fair value is not necessarily indicative of the amounts the Company could realize in a current market exchange or of future earnings or cash flows.

**VALUATION OF LONG-LIVED ASSETS**

On January 1, 2002, the Company adopted FASB Statement No. 144 *Accounting for Impairment or Disposal of Long-Lived Assets* ( FAS No. 144 ). Under FAS 144, the Company reviews long-lived assets for impairment when circumstances indicate the carrying amount of an asset may not be recoverable based on the undiscounted future cash flows of the asset. If the carrying amount of the asset is determined not to be recoverable, a write-down to fair value is recorded.

**INCOME TAXES**

Income taxes are accounted for under FASB Statement No. 109, *Accounting for Income Taxes* ( FAS 109 ). FAS 109 is an asset and liability approach that requires the recognition of deferred tax assets and liabilities for the expected future tax consequences of events that have been recognized in our financial statements or tax returns. In estimating future tax consequences, FAS 109 generally considers all expected future events other than proposed changes in the tax laws or rates. Valuation allowances are provided if it is more likely than not that a deferred tax asset will not be realized.

NET INCOME (LOSS) PER COMMON SHARE BASIC AND DILUTED

Basic earnings per share ( EPS ) is calculated by dividing the income (loss) available to common shareholders by the weighted average number of common shares outstanding for the period, without consideration for common stock equivalents. Diluted EPS gives effect to all dilutive potential common shares outstanding for the period. Shares of common stock issuable upon the exercise of options (3,462, 3,897 and 3,770 shares in 2004, 2003 and 2002, respectively) and warrants (1,742, 2,346 and 3,143 shares

## **Table of Contents**

in 2004, 2003 and 2002, respectively) and shares issued upon conversion of convertible notes (10,619, 9,859 and 9,153 in 2004, 2003 and 2002, respectively) are antidilutive and are not included in the computation of shares outstanding.

### **COMPREHENSIVE INCOME (LOSS)**

The Company follows SFAS No. 130, Reporting Comprehensive Income ( SFAS 130 ). SFAS 130 establishes standards for reporting comprehensive income or loss and its components in the consolidated financial statements. Comprehensive income (loss), as defined, includes all changes in equity (net assets) during a period from non-owner sources. To date, the Company has reported other comprehensive income from the cumulative effect on exchange rates for the amount of \$0 in 2004, \$0 in 2003 and \$(2,170) in 2002. The Company had no other material transactions that are required to be reported in comprehensive income or loss.

### **SEGMENT REPORTING**

The Company operates in one business segment the provision of telecommunication services to small and medium sized businesses on an integrated basis.

### **RECENT ACCOUNTING PRONOUNCEMENTS**

On December 16, 2004, the FASB issued Statement 123 (revised 2004) that will require compensation costs related to share-based payment transactions to be recognized in the financial statements. With limited exceptions, the amount of compensation cost will be measured based on the grant-date fair value of the equity or liability instruments issued. In addition, liability awards will be re measured each reporting period. Compensation cost will be recognized over the period that an employee provides service in exchange for the award. Statement 123(R) replaces FASB Statement No. 123, Accounting for Stock-Based Compensation, and supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees. The effective date for this requirement is as of the first interim or annual reporting period that begins after June 15, 2005. The company has not estimated the impact of adopting this revised standard on the financial statements.

In November 2004, the FASB issued SFAS No. 151, Inventory Costs an amendment of ARB No. 43, Chapter 4. SFAS No. 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs and wasted materials (or spoilage) should be recognized as current-period charges and requires the allocation of fixed production overheads to inventory based on the normal capacity of the production facilities. SFAS No. 151 is effective for fiscal years beginning after June 15, 2005. It is not expected that the adoption of SFAS No. 151 to have any effect on the Company's consolidated financial position or results of operations.

In December 2003, the FASB issued a revision to FASB Interpretation No. 46, Consolidation of Variable Interest Entities (FIN 46-R). FIN 46 is an Interpretation of Accounting Research Bulletin 51, Consolidated Financial Statements and addresses consolidation by business enterprises of variable interest entities (VIEs) that possess certain characteristics. The revision clarifies the definition in the original release that potentially could have classified any business as a VIE. The revision also delays the effective date of the Interpretation from the first reporting following December 15, 2003 to the first reporting period ending after March 15, 2004. The revision was effective for the Company in the first quarter of fiscal 2004. No VIEs have been identified and, accordingly, the application of the Interpretation did not have an effect on the Company's results of operations or financial position.

## **2. LIQUIDITY**

As reflected in the accompanying consolidated financial statements, the Company has cumulative losses and, except for the years ended December 31, 2002 and 2004, also had negative cash flows from operations.

## **Table of Contents**

Beginning in the first quarter of 2002, the Company initiated certain actions intended to improve liquidity and operating results. Such actions included, among other things, (i) completing the acquisition of Cypress Communications and making certain adjustments to Cypress Communications' staffing levels and cost structure (Note 4), (ii) liquidation of the operations in Argentina and Brazil (Note 3), (iii) completing the purchase of certain assets of Intermedia Advanced Building Networks and the shared tenant telecommunications services business of WorldCom, Inc. (Note 4), (iv) raising \$28 million in connection with such asset acquisition and (v) implementing an analysis and optimization project of our telecommunications network and real estate access costs which have resulted in substantial reductions in these cost elements in both absolute terms and as a percentage of revenue.

Cypress Holding's cash position decreased during the year ended December 31, 2004 due to one-time payments resulting from negotiated settlements on certain liabilities of Cypress Holding, related to current accrued expense, also in relation to the settlement agreements and purchases of capital equipment related to the acquisition of new customers. Management believes that Cypress Holding's cash position should stabilize during the following quarters as actions initiated in 2002 and throughout 2003 to reduce Cypress Holding's costs began to materialize starting in 2004 and resulted in the first net income from continuing operations in the Company's history. The Company is currently generating positive cash flows from operations and management believes that this trend will continue. Cypress Holding cannot, however, give any assurance that it will be able to generate sufficient cash flows from operations or financing activities to cover its future costs of operations or to operate on a profitable basis. Likewise, no assurance can be given that Cypress Holding can generate sufficient cash flow from operations or financing activities to support the debt service obligations, including debt raised in connection with its acquisition of certain assets from ABN/STS. Moreover, the terms of the indebtedness Cypress Holding incurred in connection with the acquisition of certain assets from ABN/STS contain restrictive covenants that limit its ability to incur additional indebtedness, pay dividends or undertake certain other transactions. Cypress Holding has also pledged certain assets as security under its Senior Credit Facility. Therefore, Cypress Holding must devote a substantial portion of its cash flow to service its indebtedness and cannot utilize that cash flow for operations. Accordingly, there can be no assurance that Cypress Holding will have sufficient liquidity to implement its business plan. Likewise, there can also be no assurance that Cypress Holding will be able to obtain cash through future financing activities on acceptable terms, or at all, or that Cypress Holding will ever become profitable.

As further discussed in Note 8 to these consolidated financial statements, the Company has Bridge Loan debt and fees totaling \$8,480 which will come due in July 2005. At present, the process to refinance this debt has not been initiated, pending the proposed acquisition of the Company as discussed in Note 14. Should that acquisition fail to be completed as currently contemplated, the Company would be required to either renegotiate the terms of the Bridge Loan with the current debt holders, or seek replacement financing. Failure to either renegotiate or refinance the Bridge Loan could materially affect the Company's liquidity. As a result of the aforementioned factors and related uncertainties, there is substantial doubt about the Company's ability to continue as a going concern.

### **3. DISCONTINUED OPERATIONS**

Cypress Holding discontinued and liquidated its telecommunications rights operations in Latin America during 2002. Discontinuing Cypress Holding's operations in Latin America helped Cypress Holding preserve existing capital and dedicate its resources to its new telecommunications services business in the U.S. In 2002, Cypress Holding recognized a gain from the discontinued operations of \$2,207 in connection with the discontinuation and liquidation of its Latin-American operations.

### **4. ACQUISITIONS**

### **CYPRESS COMMUNICATIONS**

In February 2002, the Company completed the acquisition of Cypress Communications, a U.S. based operation that provides a full range of telecommunications services to businesses in multi-tenant office buildings located in selected major metropolitan markets within the United States. The acquisition

**Table of Contents**

of Cypress Communications allowed the Company to concentrate its resources and expertise on providing premium communications services to over 2,500 small and medium sized business customers in seven major metropolitan U.S. markets: Atlanta, Boston, Chicago, Dallas, Houston, Los Angeles and Seattle. Cypress Communications' prior investment in telecommunications and broadband infrastructure is expected to enable the Company to provide bundled communications services to businesses located in multi-tenant office buildings in a manner that is both reliable and cost effective for its customers.

The acquisition of Cypress Communications was completed through a tender offer for outstanding Cypress Communications common stock and a short form merger of a new wholly-owned acquisition subsidiary of Cypress Holding into Cypress Communications. The purchase price was \$3.50 per share, in cash, for a total purchase price of \$18,688, which included cash paid for options to purchase shares of Cypress Communications under option plans in the amount of \$58 and expenses incurred in connection with the acquisition of \$1,447. As a result of such acquisition, the Company, at the subsidiary level, acquired 100% of Cypress Communications' assets, including cash and its telecommunications services infrastructure, and succeeded to all of the liabilities of Cypress Communications, including operating lease commitments, primarily related to former office space, and license agreements with property owners and/or operators of several office buildings. The Company obtained financing to purchase the Cypress Communications common stock and complete the merger through a loan from the LaSalle Bank, which was facilitated by the Oliver Estate, a private entity affiliated with Ross J. Mangano, a director of the Company. The loan was repaid in February 2002, with interest of approximately \$3. In connection to the loan, the Company paid a commission fee to the Oliver Estate of \$875 and issued warrants to purchase up to 850 shares of the Company's common stock at an exercise price of \$1 per share. The warrants are exercisable through February 2005 and, based on the Black-Scholes pricing model, were valued by the Company at \$646. Assumptions used for the Black-Scholes option-pricing model included: no dividend yield for all years, expected volatility of 120 percent, risk-free interest rate of 4.75 percent and expected life of 5 years. The commission and the value of the warrants were treated as interest expense in the accompanying Consolidated Statements of Operations. In addition, the Company paid bank fees and interest of approximately \$55, which also have been treated as interest expense.

The acquisition of Cypress Communications was accounted for by the purchase method of accounting and resulted in negative goodwill. The purchase price allocation, after the elimination of all long-term assets of Cypress Communications in an aggregate amount of \$26,840, resulted in an extraordinary gain associated with the acquisition in the amount of \$7,783. The consolidated statements of operations include the operations of Cypress Communications from February 1, 2002.

|                                          |           |           |
|------------------------------------------|-----------|-----------|
| ACQUISITION COSTS                        |           | \$ 18,688 |
| FAIR VALUE OF CYPRESS COMMUNICATIONS     |           | 53,311    |
| NEGATIVE GOODWILL BEFORE ASSET REDUCTION |           | (34,623)  |
| REDUCTION OF LONG TERM ASSETS            |           |           |
| Property and equipment                   | \$ 26,771 |           |
| Other assets                             | 69        | 26,840    |
| EXTRAORDINARY GAIN                       |           | \$ 7,783  |

**INTERMEDIA ADVANCED BUILDING NETWORKS**

In July 2002, the Company, through its wholly owned subsidiary, Cypress Communications, completed the purchase of certain assets of Intermedia Advanced Building Networks, the shared tenant telecommunications services



business of WorldCom, Inc (ABN/STS). The acquired assets included all customer contracts, in-building networks and the associated building access rights, as well as the necessary employees to support these assets. The acquisition of ABN/STS has allowed the Company to extend its telecommunication services operations to over 5,700 small and medium sized business customers in 25 major metropolitan U.S. markets. Cypress Communications paid \$29,000 in cash at closing to the sellers, assumed various commitments arising out of the operation of the business after the closing, assumed accrued but unpaid liabilities incurred by the sellers in the operation of the business prior to the closing in an amount up to a maximum of \$2,000, assumed vehicle lease obligations of approximately \$284 and paid

**Table of Contents**

expenses incurred in connection with the acquisition of approximately \$899. The consolidated statements of operations include the operations of ABN/STS from July 17, 2002.

The acquisition was accounted for as a purchase, and accordingly, the results of operations of ABN/STS have been included since the date of acquisition in the accompanying statements of operations. The allocation of the purchase price as of July 17, 2002 was as follows:

|                        |           |
|------------------------|-----------|
| ACQUISITION COSTS      | \$ 32,183 |
| COST ALLOCATION        |           |
| CURRENT ASSETS         | 10,662    |
| PROPERTY AND EQUIPMENT | 22,703    |
| DEFERRED REVENUES      | (1,182)   |
| TOTAL                  | \$ 32,183 |

The useful lives of the assets acquired from ABN/STS are as follows:

|                   |             |
|-------------------|-------------|
| Network Equipment | Seven years |
| Vehicles          | One year    |

Concurrently with the closing, Cypress Communications entered into an Omnibus Post-Closing Services Agreement with the sellers and certain of their affiliates. Under the Omnibus Agreement, the sellers and their affiliates agreed to provide Cypress Communications:

- (i) specified transition services;
- (ii) specified wholesale international, interstate, intrastate and local telecommunications services and Internet services (see refer to commitments under the Omnibus Post-Closing Agreement described in Note 9);
- (iii) access to the sellers' U.S. Internet collocation facilities and support services;
- (iv) access to the sellers' network collocation facilities; and
- (v) access to certain buildings of the sellers in which the purchased assets are located pending the receipt of certain consents from building owners and federal and state regulators.

In connection with such acquisition, the Company and Cypress Communications raised \$28,000 to finance the acquisition. The \$28,000 financing included:

- (i) a \$10,000 senior secured revolving credit facility from Silicon Valley Bank (the "Senior Credit Facility");
- (ii) an \$8,000 bridge loan (the "Bridge Loan") from the J. Oliver Cunningham Trust (the "JOC Trust"), the Anne C. McClure Trust (the "ACM Trust"), the Jane C. Warriner Trust (the "JCW Trust"), Noro-Moseley Partners V, L.P. (Noro-Moseley), and the Wakefield Group III, LLC (Wakefield); and

- (iii) the sale of \$10,000 of Fixed Rate Convertible Notes due July 1, 2009 (the Convertible Notes ) to the Dolphin Communications Fund II, L.P. ( Dolphin Communications ), Dolphin Communications Parallel Fund II (Netherlands), L.P. ( Dolphin Netherlands ), Noro-Moseley and Wakefield.

**Table of Contents**

The JOC Trust, the ACM Trust and the JCW Trust are affiliates of certain stockholders of the Company and of Ross J. Mangano, a director and Chairman of the Board of the Company and of Cypress Communications.

**EUREKA BROADBAND CORPORATION**

In March 2003, Cypress Holding, through Cypress Communications, acquired Eureka's Southern California building-centric voice and data services business. These assets included customer contracts, as well as Eureka's in-building networks and associated building access rights. The acquisition of the Eureka assets has allowed Cypress Holding to expand its telecommunications services operations to include over 750 small and medium sized business customers in the California market.

Cypress Holding paid \$2,500 in cash at closing to Eureka, assumed a note payable for \$500 payable six months after the acquisition based upon meeting certain operational covenants, assumed various commitments arising out of the operation of the business after the closing, assumed equipment lease obligations of approximately \$107 and paid expenses incurred in connection with the acquisition of approximately \$70. The acquired business did not meet some of the operational covenants and the Company was only required to pay \$330. The consolidated statements of operations include the operations of Eureka from April 1, 2003.

|                          |          |
|--------------------------|----------|
| ACQUISITION COSTS        | \$ 3,007 |
| COST ALLOCATION          |          |
| OTHER NON-CURRENT ASSETS | 393      |
| PROPERTY AND EQUIPMENT   | 2,614    |
| TOTAL                    | \$ 3,007 |

**E-BUILDING SOLUTIONS, INC.**

In July 2003, Cypress Holding, through Cypress Communications, negotiated the surrender of certain assets from E-Building Solutions, Inc. in California, a building-centric data services business, to mitigate the loss resulting from E-Building's default on a \$450 note due to Cypress Communications. These assets included customer contracts, as well as E-Building's in-building networks and associated building access rights. In addition to the \$450 note, Cypress Holding, assumed equipment lease obligations of approximately \$43 and paid expenses incurred in connection with the note of approximately \$43. After valuing the assets surrendered, the Company recorded a loss on investment in the amount of \$149. The consolidated statements of operations include the operations of E-Building from July 1, 2003.

|                          |        |
|--------------------------|--------|
| ACQUISITION COSTS        | \$ 536 |
| COST ALLOCATION          |        |
| OTHER NON-CURRENT ASSETS | 274    |
| PROPERTY AND EQUIPMENT   | 113    |
| LOSS ON INVESTMENT       | 149    |

TOTAL

\$ 536

**Table of Contents****5. PROPERTY AND EQUIPMENT**

Property and equipment consisted of the following at December 31, 2004 and 2003:

|                                                | 2004      | 2003      |
|------------------------------------------------|-----------|-----------|
| System infrastructure                          | \$ 31,112 | \$ 27,545 |
| Computer and office equipment                  | 1,684     | 1,277     |
| Leasehold improvements                         | 554       | 487       |
|                                                | 33,350    | 29,309    |
| Less accumulated depreciation and amortization | 9,722     | 5,060     |
|                                                | \$ 23,628 | \$ 24,249 |

**6. INTANGIBLE ASSETS**

As part of the acquisitions of the assets of Eureka and E-Building, in March and July 2003 respectively, a portion of the acquisition costs were allocated to intangible assets. The combined Gross Carrying Value for the Customer Contracts was \$567. Net Carrying Value at December 31, 2004 and 2003 was \$0 and \$239 respectively. The combined Gross Carrying Value for the Non-Compete Agreement is \$100 and the Net Carrying Value was \$42 and \$75 at December 31, 2004 and 2003 respectively.

Effective January 1, 2002, Cypress Holding adopted SFAS No. 142, *Accounting for Goodwill and Other Intangible Assets* ( SFAS No. 142 ), SFAS No. 142 requires that goodwill and certain intangible assets will no longer be subject to amortization, but instead will be subject to periodic impairment assessment by applying a fair value based test. Cypress Holding did not have any goodwill as of December 31, 2002, 2003 or 2004.

Summarized below are the carrying value and accumulated amortization of intangible assets that are to be amortized under SFAS No. 142. The Company did not have any other intangible assets as of December 31, 2002.

|                       | December 31, 2004          |                             |                       |
|-----------------------|----------------------------|-----------------------------|-----------------------|
|                       | Gross<br>Carrying<br>Value | Accumulated<br>Amortization | Net Carrying<br>Value |
| Customer Contracts    | \$ 567                     | \$ 567                      | \$ 0                  |
| Non-compete agreement | \$ 100                     | \$ 58                       | \$ 42                 |
|                       | \$ 667                     | \$ 625                      | \$ 42                 |

|                       | December 31, 2003          |                             |                       |
|-----------------------|----------------------------|-----------------------------|-----------------------|
|                       | Gross<br>Carrying<br>Value | Accumulated<br>Amortization | Net Carrying<br>Value |
| Customer Contracts    | \$ 567                     | \$ 328                      | \$ 239                |
| Non-compete agreement | \$ 100                     | \$ 25                       | \$ 75                 |

\$ 667      \$                      353      \$                      314

The estimated aggregate amortization expense for the years ended December 31, 2005 and 2006 is \$33 and \$9, respectively.

50

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**Table of Contents****7. ACCOUNTS PAYABLE AND ACCRUED EXPENSES**

Accounts payable and accrued expenses at December 31, 2004 and 2003 consist of:

|                                         | 2004      | 2003      |
|-----------------------------------------|-----------|-----------|
| Accounts payable                        | \$ 1,735  | \$ 4,886  |
| Accrued circuits and connectivity costs | 3,569     | 7,029     |
| Accrued termination charges             | 676       | 908       |
| Accrued professional fees               | 340       | 190       |
| Accrued compensation                    | 1,332     | 495       |
| Other accrued expenses                  | 2,616     | 2,836     |
|                                         | \$ 10,268 | \$ 16,344 |

Included in the above totals for the years ended December 31, 2004 and 2003 are approximately \$1,464 and \$2,700 respectively of accrued expenses which are currently in dispute with various vendors. We cannot estimate at this time the amount, if any, of these expenses that may be reduced through resolution of the various disputes. See Note 9 for further discussion of claims we made related to certain of these disputed accrued expenses.

**8. CONVERTIBLE NOTES AND DEBENTURES**

Long-term debt at December 31, 2004 and 2003 consisted of the following:

|                                                                                                                                                                                                                                                      | 2004      | 2003      |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------|-----------|
| Bridge Loan, in the amount of \$8,000, at a rate of 14% interest payable quarterly beginning September 30, 2002, with principal and any unpaid interest due July 16, 2005. (included in current installments of long term debt at December 31, 2004) | 0         | 8,280     |
| Convertible Notes including accrued interest and net of discount, with a face value of \$10,000, at a rate of 7.5%, with interest and principal due July 1, 2009.                                                                                    | 10,463    | 9,263     |
|                                                                                                                                                                                                                                                      | \$ 10,463 | \$ 17,543 |

**(a) SENIOR CREDIT FACILITY**

The Senior Credit Facility, in the amount of a \$10,000 revolving credit facility, was obtained by Cypress Communications pursuant to a Loan and Security Agreement, dated July 12, 2002 and amended in March and July of 2004 between Cypress Communications and Silicon Valley Bank. The Senior Credit Facility accrues interest at the prime rate (with a floor of 4.75%) plus 2% (7.25% as of December 31, 2004) per annum and matures on July 12, 2005, unless terminated earlier. Borrowings under the Senior Credit Facility are collateralized by all of the assets of Cypress Communications and are unconditionally guaranteed by the Company. As of December 31, 2004 and 2003, there was \$2,576 and \$2,016, respectively, outstanding under the Senior Credit Facility which has been classified as a current liability in the accompanying consolidated balance sheet.

**(b) BRIDGE LOAN**

The Bridge Loan, in the amount of \$8,000 term loan, was obtained by the Company and Cypress Communications pursuant to a Loan Agreement dated July 16, 2002 among the Company, Cypress



## **Table of Contents**

Communications, the JOC Trust, the ACM Trust, the JCW Trust, Noro-Moseley and Wakefield (each, acting in such capacity, a Bridge Lender and collectively, the Bridge Lenders ). The Bridge Loan accrues interest at 14% per annum, and matures on the earlier to occur of (i) one business day following the maturity of the Senior Credit Facility and (ii) July 16, 2005. Each Bridge Lender was entitled to receive an initial loan fee equal to 2.5% of that portion of the Bridge Loan that was funded by such Bridge Lender. Because the Bridge Loan was outstanding 60 days after the closing, the Company and Cypress Communications became obligated to pay each Bridge Lender an additional loan fee equal to 1.25% of the then outstanding principal balance of such Bridge Lender's share of the Bridge Loan. Because the Bridge Loan has been outstanding 90 days after the closing, the Company and Cypress Communications became obligated subsequent to the end of the quarterly period ended September 30, 2002 to pay each Bridge Lender an additional loan fee equal to 1.25% of the then outstanding principal balance of such Bridge Lender's share of the Bridge Loan. Because the Bridge Loan has been outstanding 120 days after the closing, the Company and Cypress Communications became obligated to pay to each Bridge Lender an additional loan fee equal to 1.00% of the then outstanding principal balance of such Bridge Lender's share of the Bridge Loan. The loan fees described above are cumulative and are payable on the earlier to occur of the maturity date of the Bridge Loans or the date on which the Bridge Loans are paid in full. The Company has accrued \$480 for these fees, which were treated as interest expense in the accompanying Consolidated Statements of Operations. The Bridge Loan, in the amount of \$8,000, has been classified as a long term liability at December 31, 2003 and as current installment of long term debt at December 31, 2004 in the accompanying balance sheets as a result of the terms of the Bridge Loan.

At the closing of the Bridge Loan, the Company issued the Bridge Lenders warrants to purchase an aggregate of 400 shares of the Company's common stock at an exercise price of \$1.13 per share. These warrants are exercisable for a term of 10 years and, based on the Black-Scholes pricing model, were valued by the Company at \$535. Assumptions used for the Black-Scholes option-pricing model included: no dividend yield for all years, expected volatility of 159 percent, risk-free interest rate of 5.08 percent and expected life of 10 years. The value of the warrants is being amortized to interest expense over two years in the accompanying Consolidated Statements of Operations.

On March 25, 2004, we amended the terms of the Bridge Loan such that, the Bridge Loan will not mature until the earlier to occur of (i) its original maturity date of July 15, 2005 or (ii) an event whereby we substantially refinance our debt obligations.

### **(c) CONVERTIBLE NOTES**

The Convertible Notes, in the amount of \$10,000, were issued by the Company and Cypress Communications pursuant to a Purchase Agreement dated July 16, 2002 among the Company, Cypress Communications, Dolphin Communications, Dolphin Netherlands, Noro-Moseley and Wakefield (each, acting in such capacity, a Purchaser and collectively, the Purchasers ). The Convertible Notes accrue interest at the rate of 7.5% per annum, compounded quarterly, and payable at maturity of the notes, whether upon their stated maturity of July 1, 2009, or earlier as a result of acceleration in the event of a default or upon redemption of the Convertible Notes. The principal of and accrued interest on the Convertible Notes is convertible into the Company's common stock at \$1.13 per share. The Convertible Notes are redeemable by the Company or Cypress Communications at any time by payment of the outstanding principal balance and accrued interest. In the event that the Convertible Notes are redeemed, the Purchasers have been issued warrants which will then be eligible for exercise to purchase the number of shares of common stock of the Issuer that the Convertible Notes were convertible into on the redemption date at a conversion price of \$1.13 per share. In connection with the issuance of the Convertible Notes, the Company, the Purchasers and the Bridge Lenders entered into a registration rights agreement, which provides for the registration of the common stock issuable upon (i) the conversion of the Convertible Notes; (ii) the exercise of the Warrants issued in connection with the Bridge Loan; and (iii) the exercise of the Warrants exercisable upon the redemption of the Convertible Notes.

In connection with the issuance of the Convertible Notes, the Purchasers were issued a total of one hundred shares of the Company's Series A Preferred Stock (the "Series A Preferred") without additional consideration. The rights of the Series A Preferred are set forth in a Certificate of Designations

## **Table of Contents**

adopted by the Company's board of directors. The holders of a majority of the Series A Preferred are entitled to elect two members of the Company's board of directors and the holders of the Series A Preferred are entitled to receive dividends and distributions equal to those payable to the holders of an equivalent number of shares of the Company's common stock. In addition, the Company may not, without the prior written consent of holders of a majority of the Series A Preferred, (i) increase or decrease (other than by redemption or conversion) the authorized number of shares of Series A Preferred; (ii) cancel or modify the voting rights of the holders of Series A Preferred; (iii) cancel or modify the rights of the holders of Series A Preferred; or (iv) amend, waive, alter, modify or repeal any provision of the Certificate of Incorporation or Bylaws of the Corporation, if such amendment, alternation, modification or repeal would adversely affect the Series A Preferred, including the issuance of preferred stock with voting rights senior to or pari passu with the Series A Preferred. The Series A Preferred is redeemable by the Company in the event that:

- (i) at least 75% of the principal amount of the Convertible Notes is converted into shares of common stock of the Company;
- (ii) at least 75% of the principal amount of the Convertible Notes is redeemed;
- (iii) the Company has submitted an application in good faith to apply for listing on AMEX, NASDAQ or another national exchange to register its securities on such exchange, the average daily trading price per share of the common stock as reported in such application is at least \$4.00 per share, and the Company subsequently receives a comment from such exchange that its application for listing will not be accepted so long as the Series A Preferred remains outstanding with the voting rights described herein; or
- (iv) the outstanding principal and interest on the Convertible Notes are paid in full on the maturity date of the Convertible Notes.

The redemption price for the Series A Preferred is \$0.001 per share.

At the closing of the Convertible Notes, the Company issued the Convertible Note Lenders warrants to purchase the number of shares of the Company's common stock in to which the Convertible Notes would be convertible immediately prior to the redemption of such note at a price of \$1.13 per share. These warrants are exercisable if the Convertible Notes are redeemed and have a life of 7 years. The Company will not record any charge until the notes are redeemed. The Company has estimated that based on the terms of the Convertible Notes that if the Company redeemed the Convertible Notes it would redeem the entire amount. Therefore, based on the Black-Scholes pricing model, the warrants were valued by the Company at \$12,035. Assumptions used for the Black-Scholes option-pricing model included: no dividend yield for all years, expected volatility of 159 percent, risk-free interest rate of 4.81 percent and expected life of 7 years.

The Bridge Lenders and the Purchasers entered into an Intercreditor (Subordination) Agreement, which, among other things, provides that under certain limited circumstances, all amounts payable by the Company and Cypress Communications under the Bridge Loan and the Convertible Notes will be payable, pro rata among the Bridge Lenders and the Purchasers, on a pari passu basis. To induce the JOC Trust, the ACM Trust and the JCW Trust to enter into the Intercreditor (Subordination) Agreement, the Company and Cypress Communications entered into a Letter Agreement. Pursuant to the Letter Agreement, the Company and Cypress Communications agreed to pay the Bridge Lenders and the Purchasers, in proportion to the amounts lent by them under the Bridge Loan, a fee of \$1,000 (the Risk Allocation Fee). The Risk Allocation Fee was to be payable to certain Bridge Lenders and the Purchasers upon the earlier to occur of the achievement of certain earnings milestones set forth in the Letter Agreement or June 30, 2003. In December 2002, the Company agreed to accelerate the payment terms for this Risk Allocation Fee, issuing a payment of \$915 in settlement of the full outstanding amount. The Company recognized the \$85 difference in 2002 as an extraordinary gain on extinguishment of debt.

As the exercise price of the Convertible Notes of \$1.13 was less than the relative fair market value of the stock as of the consummation date, a beneficial conversion was created. The Company has

**Table of Contents**

calculated the beneficial conversion feature embedded in the Convertible Notes in accordance with EITF No. 98-5 and EITF No. 00-27 and recorded approximately \$2,389 as a debt discount. This discount is being amortized over the seven-year life of the Convertible Notes. During the year ended December 31, 2004, 2003 and 2002, the Company recorded \$341, \$341 and \$171 respectively, in additional interest expense.

**FUTURE ANNUAL COMMITMENTS**

Future annual payments under capital leases and long-term debt as of December 31, 2004 are as follows:

|                      |           |
|----------------------|-----------|
| 2005                 | 8,511     |
| 2006                 | 4         |
| 2007                 |           |
| 2008                 |           |
| 2009                 | 12,000    |
| Total                | 20,515    |
| Less current portion | (8,511)   |
| Long-term portion    | \$ 12,004 |

**9. COMMITMENTS AND CONTINGENCIES****(a) LEASES**

Cypress Holding is obligated under several operating lease agreements for office space, including switch room space in the buildings where we have licenses to provide our services. Future annual minimum rental payments under these leases as of December 31, 2004 are as follows:

|            | Gross<br>minimum<br>rental<br>payments | Cash due<br>under<br>subleases | Net minimum<br>rental<br>payments |
|------------|----------------------------------------|--------------------------------|-----------------------------------|
| 2005       | 5,728                                  | 1,010                          | 4,718                             |
| 2006       | 3,731                                  | 551                            | 3,180                             |
| 2007       | 2,279                                  | 274                            | 2,005                             |
| 2008       | 921                                    | 41                             | 880                               |
| 2009       | 547                                    | 35                             | 512                               |
| Thereafter | 197                                    | 35                             | 162                               |
| Total      | \$ 13,403                              | \$ 1,946                       | \$ 11,457                         |

Rent expense for 2004, 2003 and 2002 was approximately \$6,318, \$6,776, and \$4,041, respectively.

**(b) OBLIGATIONS UNDER LICENSE AGREEMENTS**

Cypress Holding has entered into license agreements with property owners and/or operators of several office buildings whereby Cypress Holding has the right to provide communications services in these buildings. Under the

terms of the agreements, Cypress Holding is generally obligated to pay a commission based on the greater of a base fee or a percentage of revenue earned in the related building or development. At December 31, 2004, Cypress Holding's aggregate minimum obligations under these agreements were as follows:

**Table of Contents**

|            |          |
|------------|----------|
| 2005       | 1,120    |
| 2006       | 943      |
| 2007       | 824      |
| 2008       | 644      |
| 2009       | 466      |
| Thereafter | 495      |
| Total      | \$ 4,492 |

The commitments above exclude an estimated total of \$1.2 million of potential obligations under license agreements in buildings in which Cypress Holding's communications network has not been constructed. In the opinion of management, such amounts will not be owed, as Cypress Holding is not providing services in those buildings.

License expense for 2004, 2003 and 2002 was approximately \$4,126, \$4,123 and \$2,676 respectively, included in direct costs in the consolidated statement of operations.

**(c) OBLIGATIONS UNDER COMMUNICATIONS SERVICE AGREEMENTS**

At December 31, 2004, Cypress Holding had contracts with some communications providers with minimum purchase obligations for leased voice and data transport and other services. As of December 31, 2004, approximate future minimum purchase commitments under these agreements were as follows:

|       |           |
|-------|-----------|
| 2005  | \$ 10,311 |
| 2006  | 72        |
| 2007  | 66        |
| Total | \$ 10,449 |

Expense for leased voice and data transport under communications service agreements for 2004, 2003 and 2002 was approximately \$24,985, \$32,575 and \$34,943 respectively, included in direct costs in the consolidated statement of operations.

**(d) LEGAL PROCEEDINGS**

Cypress Holding is subject to legal proceedings and claims, including employment and other matters that arise in the ordinary course of business. Except as set forth below, there are no pending legal proceedings to which Cypress Holding is a party that management believes will have a material adverse effect on the financial position, results of operations, or cash flows of Cypress Holding.

With respect to the Company's ABN/STS acquisition referenced in Note 4, on or about January 23, 2003, the Company filed proofs of claim in the bankruptcy cases of WorldCom, Inc. and certain of its debtor affiliates as a result of the Debtors' defaults under that certain Asset Purchase Agreement dated May 31, 2002 by and among Intermedia Communications, Inc., Shared Technologies Fairchild, Inc., Shared Technologies Fairfield Telecom, Inc., MCI Worldcom Communications, Inc., Worldcom, Inc., MCI-WORLDCOM Network Services, Inc. (the Debtors) and Cypress Communications, that certain Omnibus Post-Closing Agreement dated July 16, 2002, by and among the Debtors and Cypress Communications and certain other related ancillary documents (collectively the Transaction Documents). The Company filed amendments to these proofs of claim on January 29, 2004 to increase our claim to \$13,852, which amended proofs of claim include damages caused to us as a result of certain fraudulent accounting practices of the Debtors (not, so far as the Company is aware, specific to Cypress Communications) and failure to perform required actions and other breaches of the Transaction Documents by the Debtors.

On or about October 18, 2004, the Debtors objected to the Company's proofs of claim and a hearing has been set for April 22, 2005. The Company expects that WorldCom will bring counterclaims



**Table of Contents**

alleging breaches by Cypress of the agreements and related ancillary documents. The Company expects such counterclaims may seek damages of approximately \$2,300, of which the Company has \$1,464 million currently recorded in accrued expenses. The Company cannot express an opinion as to whether a favorable or unfavorable outcome is either probable or remote or to estimate the range of any possible loss or gain that may result from the settlement of these claims. An unfavorable outcome could, under certain circumstances, result in a material adverse effect on our business, financial condition and results of operations.

(e) TELECOMMUNICATIONS TAXES PAID

During the quarter ended September 30, 2004, management determined that the Company made payments to telecommunications service providers for federal, state and local taxes and surcharges on telecommunications services for which it might be exempt. The Company is attempting to recover these taxes and surcharges directly from the telecommunications service providers involved. Although management believes that the amount of taxes and surcharges which the Company is entitled to recover is in the range of \$1,000 to \$2,500, there is no assurance that any amounts will be recovered or when any amounts will be recovered, if ever. The recovery of these taxes and surcharges will be recorded in the financial statements when the taxes and surcharges are actually recovered. From December 31, 2004 to March 1, 2005, the Company has recovered approximately \$200 in telecommunications taxes from its vendors.

10. STOCKHOLDERS EQUITY

(a) EMPLOYEE EQUITY INCENTIVE PLAN

In April 1999, the Company's Board of Directors approved a 10-year Employee Equity Incentive Plan, subject to approval of its stockholders. The stockholders ratified the Plan in September 1999.

In March 2002, the Company's board of directors approved an amendment to the 1999 Employee Equity Incentive Plan (the "Option Plan"). By this amendment, the number of shares of common stock reserved for issuance under the Option Plan was increased to 3,200 shares, subject to automatic annual adjustment to an amount equal to 30% of our outstanding common stock on a fully diluted basis, up to a maximum of 5,000. The amendment was approved by the Company's shareholders at the Annual Meeting of Shareholders on June 26, 2002.

In August 2002, the Company's board of directors approved a second amendment to the Option Plan. By this amendment, the number of shares of common stock reserved for issuance under the Option Plan was increased to 4,200 shares, subject to the existing automatic annual adjustment contained in the Option Plan, and increasing to 1,500 the aggregate limit on the number of options that may be granted to any one optionee during the term of the Option Plan. As of December 31, 2004, after giving effect to the issuance of additional options following adoption of the amendment, options to purchase 3,462 shares were outstanding under such plan.

**Table of Contents**

The following table summarizes the Company's employee stock option activity:

|                                  | Shares  | Weighted<br>Average<br>Exercise<br>Price | Shares | Exercisable<br>Weighted<br>Average<br>Exercise<br>Price |
|----------------------------------|---------|------------------------------------------|--------|---------------------------------------------------------|
| Outstanding at December 31, 2001 | 537     | \$ 6.87                                  | 537    | \$ 6.87                                                 |
| 2002:                            |         |                                          |        |                                                         |
| Granted                          | 3,495   | \$ 1.74                                  |        |                                                         |
| Forfeited                        | (207)   | \$ 1.52                                  |        |                                                         |
| Outstanding at December 31, 2002 | 3,825   | \$ 2.48                                  | 537    | \$ 6.87                                                 |
| 2003:                            |         |                                          |        |                                                         |
| Granted                          | 487     | \$ 1.38                                  |        |                                                         |
| Forfeited                        | (415)   | \$ 3.39                                  |        |                                                         |
| Outstanding at December 31, 2003 | 3,897   | \$ 2.24                                  | 1,732  | \$ 2.95                                                 |
| 2004:                            |         |                                          |        |                                                         |
| Granted                          | 726     | \$ 1.25                                  |        |                                                         |
| Forfeited                        | (1,161) | \$ 3.45                                  |        |                                                         |
| Outstanding at December 31, 2004 | 3,462   | \$ 1.60                                  | 1,821  | \$ 1.72                                                 |

The following table summarizes information about the stock options outstanding at December 31, 2004:

| Exercise Price | Number of<br>Options<br>Outstanding<br>at<br>December 31,<br>2004 | Weighted<br>Average<br>Remaining<br>Contractual<br>Life (in Years) | Weighted<br>Average<br>Exercise<br>Price | Exercisable<br>as of<br>December 31,<br>2004 |
|----------------|-------------------------------------------------------------------|--------------------------------------------------------------------|------------------------------------------|----------------------------------------------|
| \$1.25         | 1,127                                                             | 9                                                                  | \$ 1.25                                  | 100                                          |
| \$1.50 \$1.60  | 1,230                                                             | 5                                                                  | \$ 1.50                                  | 1,030                                        |
| \$2.00         | 1,095                                                             | 7                                                                  | \$ 2.00                                  | 681                                          |
| \$10.00        | 10                                                                | 1                                                                  | \$ 10.00                                 | 10                                           |
|                | 3,462                                                             | 7                                                                  | \$ 1.72                                  | 1,821                                        |

## (b) NON-CASH EQUITY TRANSACTIONS

The Company valued warrants issued during the year ended December 31, 2002 in connection with financing agreements at \$1,181, using the Black-Scholes pricing model. Warrants issued to purchase up to 850 shares of the Company's common stock at an exercise price of \$1 per share, were valued at \$646, assuming: no dividend yield for all years, expected volatility of 120 percent, risk-free interest rate of 4.75 percent and expected life of 5 years. Warrants to purchase 400 shares of the Company's common stock at an exercise price of \$1.13 per share were valued at \$535, assuming: no dividend yield for all years, expected volatility of 159 percent, risk-free interest rate of 5.08 percent and expected life of 10 years.

No such transactions were recorded during the years ended December 31, 2004 and 2003. The \$1,181 amount in 2002 was charged to interest expense.

(c) STOCK OPTIONS AND WARRANTS OUTSTANDING

All stock options and warrants issued before 2001 are currently exercisable. Stock options issued in 2001 vest ratably over three years, and stock options issued in 2002 and beyond vest ratably over four

**Table of Contents**

years, with the exception of 1,900 issued to the Company's current and former Chief Executive Officer's in 2002, which vest 50% upon the achievement by the Company of positive cash flow for 4 consecutive quarters on a cumulative basis, 25% on the first anniversary of the vesting of the initial 50%, and 25% on the second anniversary of the vesting of the initial 50%. Certain members of the executive management of the Company were awarded performance-based options on March 20, 2002 (the "March Options") and August 6, 2002 (the "August Options"). The purpose of these performance-based options was to better align executive management's compensation with growth of the Company. Both the March Options and August Options vest (1) 50% upon the achievement of four consecutive quarters of positive cash flow, on a cumulative basis, as defined in the option agreements (the "First Performance Date"), (2) 25% upon the first anniversary of the First Performance Date, and (3) 25% on the second anniversary of the First Performance Date. The options have a ten-year life and were issued with an exercise price above the fair value of the underlying stock on the date of the grant. The Company follows APB Opinion Number 25, "Accounting for Stock Issued to Employees," and, accordingly, compensation expense for stock options is measured as the excess, if any, of the fair value of the Company's stock at the measurement date over the exercise price.

During the second quarter of 2003, the Company achieved the cash flow performance for the March Options and established the First Performance Date for the March Options. Accordingly, the first 50% of the March Options vested in accordance with the terms of the option agreement. The Company has recorded compensation expense in 2004, 2003 and 2002 in the amount of \$78, \$438 and \$0 in connection with the March Options, which includes the cost related to the 50% vested during the period and a prorated amount for the 50% to be vested over the next two years according to the agreement. During 2004, coincident with the Chief Executive Officer leaving the Company, the amortization of compensation expense related to his portion of the March Options was halted. Upon his departure, the Chief Executive Officer forfeited 550 unvested options granted in 2002. The Company will expense the remaining compensation cost for the other executive over the vesting period.

In connection with the August Options, the Company has not recorded any stock compensation expense, as the exercise price of the performance-based options is \$2.00, which is currently in excess of the fair market value of the stock.

The stock options and warrants expire as follows:

|            | <b>Year Ending December 31, 2004</b> | <b>Shares</b> | <b>Weighted<br/>Average<br/>Exercise<br/>Price</b> |
|------------|--------------------------------------|---------------|----------------------------------------------------|
| 2005       |                                      | 1,902         | \$ 1.85                                            |
| 2006       |                                      |               |                                                    |
| 2007       |                                      | 10            | \$ 1.60                                            |
| 2008       |                                      | 10            | \$ 1.60                                            |
| 2009       |                                      | 10,629        | \$ 1.13                                            |
| Thereafter |                                      | 3,461         | \$ 1.52                                            |
|            |                                      | 16,012        | \$ 1.30                                            |

**11. TREASURY STOCK**

In July 2001, the Company purchased for approximately \$800 an aggregate of 533 shares of the Company's common stock from a former Company director and members of his family. On April 1, 2002, Cypress Holding

announced that its Board of Directors had approved the use of up to \$500 for repurchase of its common stock. Under this stock repurchase program, as of December 31, 2004, the Company had purchased approximately 61 shares of the Company's common stock at fair value for approximately \$60. The shares were accounted for as treasury stock and are shown separately as a deduction from the total common stock.

**Table of Contents****12. RELATED PARTY TRANSACTIONS**

In February 2002, the Company entered into severance arrangements with certain officers and employees of the Company. Under these arrangements, the Company paid out severance of approximately \$400 during the first quarter of 2002.

See also Notes 8(b) and (c) for interim bridge financing and a convertible note payable with related parties, equity securities issued to related parties and subsequent event, respectively.

**13. INCOME TAXES**

The benefit/(provision) for income taxes from continuing operations consisted of the following for the years ended December 31, 2004, 2003 and 2002:

|                                            | 2004    | 2003    | 2002    |
|--------------------------------------------|---------|---------|---------|
| Current                                    | \$      | \$      | \$      |
| Deferred                                   | (3,462) | 1,602   | 5,573   |
| (Increase)/Decrease in valuation allowance | 3,462   | (1,602) | (5,573) |
| Income tax benefit / (provision)           | \$      | \$      | \$      |

Deferred income taxes reflect the net tax effect of temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The significant components of deferred tax assets and liabilities as of as of December 31, 2004, 2003 and 2002 are as follows:

|                                       | 2004       | 2003       | 2002       |
|---------------------------------------|------------|------------|------------|
| Non-current deferred tax assets:      |            |            |            |
| Net operating loss carryforwards      | \$ 150,694 | \$ 137,344 | \$ 96,999  |
| Allowance for doubtful accounts       | 83         | 161        | 411        |
| Acquired liabilities accrual          | 271        | 402        | 8,371      |
| Real estate access rights             | 32,306     | 39,520     | 46,734     |
| Property, plant & equipment           | 10,367     | 19,785     | 15,395     |
| Stock Based compensation              | 454        | 423        |            |
| Other Intangible assets               | 19         | 21         | 311        |
| Total non-current deferred tax assets | \$ 194,194 | \$ 197,656 | \$ 168,249 |
| Net deferred income taxes:            |            |            |            |
| Valuation allowance                   | (194,194)  | (197,656)  | (168,249)  |
| Net deferred income taxes             | \$         | \$         | \$         |

At December 31, 2004, Cypress Communications had available federal net operating loss carry forwards of approximately \$386,000 that expire from 2012 to 2024. The utilization of \$223,000 of these loss carry forwards is subject to an annual limitation as a result of a change in ownership of Cypress Communications, as defined in the Internal Revenue Code. The limitation does not reduce the total amount of net operating losses that may be taken, but rather substantially limits the amount that may be used during a particular year. Cypress Communications also had various state net operating loss carry forwards that expire from 2012 to 2024. Management has reviewed the net deferred tax assets as of December 31, 2004, and determined that it is more likely than not that all of the deferred tax

assets will not be realized. The amount of the valuation allowance has decreased as of December 31, 2004, due to changes in deferred tax balances relative to real estate access rights and property, plant and equipment.

**Table of Contents**

A reconciliation of the income tax provision computed at statutory tax rates to the income tax provision for the years ended December 31, 2004, 2003 and 2002 is as follows:

|                                                | 2004    |        | 2003       |       | 2002       |         |
|------------------------------------------------|---------|--------|------------|-------|------------|---------|
| Income tax expense/(benefit) at statutory rate | \$ 148  | 35%    | \$ (1,438) | (35)% | \$ (3,998) | (35)%   |
| State income taxes, net of federal benefit     | 17      | 4%     | (164)      | (4)%  | (456)      | (4)%    |
| Reduction in NOL Carryover                     | 3,258   | 770%   |            |       |            |         |
| Meals & Entertainment & Penalties              | 39      | 9%     |            | %     | (1,119)    | (1.85)% |
| Increase/(decrease) in valuation allowance     | (3,462) | (818)% | 1,602      | 39%   | 5,573      | 40.85%  |
| Income tax provision/(benefit)                 |         |        |            |       |            |         |

**14. EMPLOYEE BENEFIT PLAN**

The Company has a 401(k) Profit Sharing Plan (the Plan) for the benefit of eligible employees and their beneficiaries. All employees are eligible to participate on the first full month following the date of employment. The Company did not make any matching contributions in 2004 or in any of the prior periods presented.

**15. PENDING ACQUISITION OF THE COMPANY**

On November 5, 2004, Cypress Holding, TechInvest Holding Company, Inc., an affiliate of Arcapita Inc. ( Parent ), and TechInvest Acquisition, Inc., a wholly-owned subsidiary of Parent ( Purchaser ), entered into an Agreement and Plan of Merger (the Merger Agreement) pursuant to which Parent will acquire Cypress Holding by the merger of Purchaser with and into Cypress Holding, with Cypress Holding surviving the merger as a wholly-owned subsidiary of Parent. The total value of the transaction, at the time of the execution of the Merger Agreement, was \$39,350. The Merger Agreement contains provisions for final merger consideration adjustments, upwards or downwards, based on the achievement of certain conditions pertaining to changes in certain current assets and liabilities between the execution of the Merger Agreement and closing of the transaction.

On February 3, 2005, in recognition of the potential increase in working capital relating to the telecommunications tax recovery, Cypress Holding and Parent agreed to amend the Merger Agreement (the Amendment) to increase the merger consideration by \$935, making the total value of the transaction \$40,285. The parties also agreed in the Amendment, among other things, that accounts receivable attributable to the telecommunications tax recovery will be capped in light of the increase in the merger consideration for purposes of calculating the final merger consideration adjustment.

The Merger Agreement provides that the merger consideration will first be used to repay outstanding indebtedness. The remaining consideration, after transaction expenses, will be distributed to stockholders, with an estimated price per share of \$1.71, subject to final merger consideration adjustments (The \$1.71 per share cash consideration is estimated by Cypress Holding as of December 31, 2004 and is subject to adjustment upwards or downwards pursuant to the merger agreement).

The closing of the transaction is subject to certain terms and conditions customary for transactions of this type, including receipt of stockholder and regulatory approvals and other conditions.



On March 15, 2005, a majority of the shareholders of each class of the Company's voting stock voted to approve the Merger Agreement

**Table of Contents**

The Company incurred \$597 in expenses during 2004 related to the solicitation, negotiation and completion of the sale transaction, which are recorded in general and administrative expense in the consolidated statement of operations.

**16. SUBSEQUENT EVENTS**

In January 2005, a shareholder exercised outstanding warrants to purchase 850 shares of the Company's Common Stock through payment to the Company of \$850.

In March 2005, a former employee exercised options to purchase 400 shares of the Company's Common Stock through payment to the Company of \$600.

**17. QUARTER-BY-QUARTER COMPARISON (UNAUDITED) (In thousands, except per share data)**

|                                                      | First     | Second    | Third     | Fourth    |
|------------------------------------------------------|-----------|-----------|-----------|-----------|
| 2004                                                 |           |           |           |           |
| Operating revenues                                   | \$ 19,884 | \$ 20,271 | \$ 19,433 | \$ 19,394 |
| Net Income (Loss)                                    | (631)     | 664       | 303       | 87        |
| Basic Income (Loss) per share                        | (0.11)    | 0.11      | 0.05      | 0.01      |
| Diluted Income (Loss) per share                      | (0.11)    | 0.11      | 0.05      | 0.01      |
| Weighted Average Common Shares Outstanding (basic)   | 5,874     | 5,874     | 5,874     | 5,874     |
| Weighted Average Common Shares Outstanding (diluted) | 5,874     | 5,874     | 5,874     | 7,810     |
|                                                      | First     | Second    | Third     | Fourth    |
| 2003                                                 |           |           |           |           |
| Operating revenues                                   | \$ 21,964 | \$ 21,808 | \$ 21,046 | \$ 19,808 |
| Net Income (Loss)                                    | (1,148)   | (56)      | (1,830)   | (1,129)   |
| Per common share Basic and Diluted                   |           |           |           |           |
| Basic and Diluted Loss per share                     | (0.20)    | (0.01)    | (0.31)    | (0.19)    |
| Weighted Average Common Shares Outstanding           | 5,874     | 5,874     | 5,874     | 5,874     |

**Table of Contents**

Report of Independent Registered Public Accounting Firm

Cypress Communications, Inc.

We have audited the accompanying consolidated statements of operations, changes in stockholders' equity and cash flows of Cypress Communications, Inc. and subsidiaries for the one-month period from January 1, 2002 to January 31, 2002. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with auditing standards of the Public Company Accounting Oversight Board (United States) generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the results of its operations and cash flows for the one-month period from January 1, 2002 to January 31, 2002, in conformity with accounting principles generally accepted in the United States of America.

/s/ Deloitte & Touche, LLP

Atlanta, Georgia  
April 1, 2003

**Table of Contents**

CYPRESS COMMUNICATIONS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF OPERATIONS

FOR THE ONE-MONTH PERIOD FROM JANUARY 1, 2002 TO JANUARY 31, 2002

|                                  |                |
|----------------------------------|----------------|
| REVENUES                         | \$ 1,565,000   |
| DIRECT COSTS                     | 1,318,000      |
| REVENUES NET OF DIRECT COSTS     | 247,000        |
| OPERATING EXPENSES               |                |
| Sales and Marketing              | 270,000        |
| General and administrative       | 7,770,000      |
| TOTAL OPERATING EXPENSES         | 8,020,000      |
| Loss from continuing operations  | (7,773,000)    |
| OTHER INCOME (EXPENSE)           |                |
| Interest income                  | 85,000         |
| Interest expense                 | (17,000)       |
| TOTAL OTHER INCOME (EXPENSE) NET | 68,000         |
| Loss before income taxes         | (7,705,000)    |
| Income tax                       |                |
| Net Loss                         | \$ (7,705,000) |

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Table of Contents

## CYPRESS COMMUNICATIONS, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY

FOR THE ONE-MONTH PERIOD FROM JANUARY 1, 2002 TO JANUARY 31, 2002

|                                                 | Shares    |          | Additional<br>Paid-In<br>Capital | Deferred<br>Compen-<br>sation | Other<br>Compre-<br>hensive<br>Income<br>(Loss) | Accu-<br>mulated<br>Deficit | Stock-<br>holders<br>Equity | Compre-<br>hensive<br>Loss |
|-------------------------------------------------|-----------|----------|----------------------------------|-------------------------------|-------------------------------------------------|-----------------------------|-----------------------------|----------------------------|
| BALANCE,<br>January 1,<br>2002                  | 4,926,000 | \$ 6,000 | \$ 569,827,000                   | \$ (6,312,000)                | \$ (47,000)                                     | \$ (508,739,000)            | \$ 54,735,000               | \$                         |
| Write-off of<br>deferred<br>compensation        |           |          |                                  | 6,312,000                     |                                                 |                             | 6,312,000                   |                            |
| Unrealized loss<br>on short-term<br>investments |           |          |                                  |                               | (31,000)                                        |                             | (31,000)                    | (31,000)                   |
| Net loss                                        |           |          |                                  |                               |                                                 | (7,705,000)                 | (7,705,000)                 | (7,705,000)                |
| Comprehensive<br>loss                           |           |          |                                  |                               |                                                 |                             |                             | \$ (7,736,000)             |
| BALANCE,<br>January 31,<br>2002                 | 4,926,000 | \$ 6,000 | \$ 569,827,000                   | \$                            | \$ (78,000)                                     | \$ (516,444,000)            | \$ 54,735,000               |                            |

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Table of Contents**

CYPRESS COMMUNICATIONS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS

FOR THE ONE-MONTH PERIOD FROM JANUARY 1, 2002 TO JANUARY 31, 2002

CASH FLOWS FROM OPERATING ACTIVITIES:

|                                                                             |                |
|-----------------------------------------------------------------------------|----------------|
| Net loss                                                                    | \$ (7,705,000) |
| Adjustments to reconcile net loss to net cash used in operating activities: |                |
| Depreciation and amortization                                               | 321,000        |
| Write-off of deferred compensation                                          | 6,312,000      |
| Bad debt expense                                                            | 8,000          |
| Other non cash item                                                         | (31,000)       |
| Changes in operating assets and liabilities:                                |                |
| Accounts receivable, net                                                    | (89,000)       |
| Prepaid expenses and other current assets                                   | (831,000)      |
| Other assets                                                                | 780,000        |
| Accounts payable and accrued expenses                                       | (908,000)      |
| Deferred revenues                                                           | 282,000        |
| Net cash used in operating activities                                       | (1,855,000)    |

CASH FLOWS FROM INVESTING ACTIVITIES:

|                                           |       |
|-------------------------------------------|-------|
| Sale of property and equipment            | 8,000 |
| Net cash provided by investing activities | 8,000 |

CASH FLOWS FROM FINANCING ACTIVITIES:

|                                                 |  |
|-------------------------------------------------|--|
| Principal payments on capital lease obligations |  |
| Net cash used in financing activities           |  |

|                                               |               |
|-----------------------------------------------|---------------|
| DECREASE IN CASH AND CASH EQUIVALENTS         | (1,847,000)   |
| CASH AND CASH EQUIVALENTS, BEGINNING OF MONTH | 33,757,000    |
| CASH AND CASH EQUIVALENTS, END OF MONTH       | \$ 33,910,000 |

SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:

|                        |           |
|------------------------|-----------|
| Cash paid for interest | \$ 17,000 |
|------------------------|-----------|

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**Table of Contents**

**CYPRESS COMMUNICATIONS, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE ONE-MONTH PERIOD FROM JANUARY 1, 2002 TO JANUARY 31, 2002**

**1. ORGANIZATION AND NATURE OF BUSINESS**

Cypress Communications, Inc. and its subsidiaries ( Cypress Communications or the Company ) provide a full range of communications services to businesses in multi-tenant office buildings located in select major metropolitan markets within the United States. In February 2002, the Company was acquired by Cypress Communications Holding Co., Inc. ( Cypress Holding ). The Company's communications services include high speed Internet access and data services, local and long-distance voice services, feature-rich digital telephone systems, digital satellite business television, voicemail, e-mail, web site hosting, security/monitoring services, and other advanced communications services. The Company delivers these services over state-of-the-art fiber optic, digital, and broadband networks that Cypress Communications designs, constructs, owns, and operates inside large- and medium-sized office buildings.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**BASIS OF PRESENTATION**

The accompanying financial statements are presented on the accrual basis of accounting using accounting principles generally accepted in the United States.

**PRINCIPLES OF CONSOLIDATION**

The consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly owned. All significant intercompany transactions and balances have been eliminated in consolidation.

**ACCOUNTING ESTIMATES**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States 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 dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual amounts could differ from these estimates, and such differences could be material.

**REVENUE RECOGNITION**

The Company's revenues include recurring charges for local access, long-distance, equipment rental, Internet access, digital satellite business television, voicemail, inbound 800, and other enhanced voice and data services, which are recognized as services are provided. Revenues also include nonrecurring charges for installations and moves, adds, and changes. Installation fees represent the initial cost charged by Cypress Communications for installing voice phone lines, data lines, and Business TV in the tenant's premises. Move, add, and change ( MAC ) charges are for the Company's labor and materials related to moving, adding, or changing a customer's services. Installation and certain MAC charges are recognized when the services are provided as they represent separate earnings process. Other MAC charges, which are not separate earnings process, are generally deferred and amortized over 24 months.





**Table of Contents**

**CASH AND CASH EQUIVALENTS**

The Company considers all highly liquid instruments with an original maturity of three months or less to be cash equivalents.

**PROPERTY AND EQUIPMENT**

Depreciation is computed using the straight-line method over the estimated useful lives of the assets (generally three to seven years). Leasehold improvements are depreciated over the lesser of the average lease term (or the term of the related license agreement) or the assets' useful lives. Depreciation expense was \$321,000 for the one-month period ended January 31, 2002. Maintenance and repairs are charged to expense as incurred. Gains or losses on disposal of property and equipment are recognized in operations in the year of disposition.

**DEFERRED COMPENSATION**

Deferred compensation has been expensed in the one-month period ended January 31, 2002 due to the acceleration of vesting provision of the underlying equity instrument in connection with the acquisition by Cypress Holding (note 5).

**SEGMENT REPORTING**

The Company provides an integrated package of communication products to small- and medium-sized businesses and manages its business on an integrated basis.

**RECENT ACCOUNTING PRONOUNCEMENTS**

In April 2002, the FASB issued SFAS 145, *Rescission of FASB Statements SFAS 4, 44 and 64, Amendment of FASB Statement No. 13 and Technical corrections*. This Statement rescinded Statement No. 4, Reporting Gains and Losses from Extinguishments of Debt, and an amendment of that Statement, FASB Statement No. 64, Extinguishments of Debt Made to Satisfy Sinking-Fund Requirements. This Statement also rescinded FASB Statement No. 44, Accounting for Intangible Assets of Motor Carriers. This Statement amended FASB Statement No. 13, Accounting for Leases, to eliminate an inconsistency between the required accounting for sale-leaseback transactions and the required accounting for certain lease modifications that have economic effects that are similar to sale-leaseback transactions. This Statement also amended other existing authoritative pronouncements to make various technical corrections, clarify meanings, or describe their applicability under changed conditions. The provision of this Statement related to the rescission of Statement No. 4 must be applied in fiscal year beginning after May 15, 2002. The provisions of this Statement related to Statement 13 will be applicable for transactions occurring after May 15, 2002. Early application of the provisions of this Statement is encouraged. The Company does not expect the adoption of SFAS 145 will have a significant impact on its consolidated results of operations, financial position or cash flows.

In June 2002, the FASB issued SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*. SFAS No. 146 requires the recording of costs associated with exit or disposal activities at their fair values when a liability has been incurred. Under previous guidance, certain exit costs were accrued upon management's commitment to an exit plan, which is generally before an actual liability has been incurred. SFAS No. 146 is to be applied prospectively to exit or disposal activities initiated after December 31, 2002. The Company does not expect the adoption of SFAS 146 will have a significant impact on its consolidated results of operations, financial position or cash flows.

In November 2002, the FASB issued Interpretation (FIN) No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantors, Including Indirect Guarantees of Indebtedness of Others*. FIN No. 45 requires that upon issuance of a guarantee, the guarantor must recognize a liability for the fair value of the obligation it assumes under the guarantee. Guarantors will also be required to meet expanded

**Table of Contents**

disclosure obligations. The initial recognition and measurement provisions of FIN No. 45 are effective for guarantees issued or modified after December 31, 2002. The disclosure requirements are effective for annual and interim financial statements that end after December 15, 2002. The Company does not believe the adoption of FIN 45 will have a material impact on its consolidated financial statements.

**3. COMMITMENTS AND CONTINGENCIES****LEASES**

The Company is obligated under several operating and capital lease agreements, primarily for office space and equipment. Future annual minimum rental payments assumed on December 31 year-end under these leases as of January 31, 2002 are as follows:

|                                                        | <b>Operating</b> | <b>Capital</b> |
|--------------------------------------------------------|------------------|----------------|
| 2002                                                   | 2,756,000        | \$ 473,000     |
| 2003                                                   | 3,124,000        | 327,000        |
| 2004                                                   | 3,224,000        | 25,000         |
| 2005                                                   | 2,836,000        | 16,000         |
| 2006                                                   | 1,662,000        | 0              |
| Thereafter                                             | 903,000          | 0              |
| Total                                                  | 14,505,000       | 841,000        |
| Less amount representing interest and taxes            |                  | 97,000         |
| Present value of future minimum capital lease payments |                  | 744,000        |
| Less current portion                                   |                  | (409,000)      |
| Long-term portion                                      |                  | \$ 335,000     |

Minimum commitments under operating leases above are net of cash due to the Company under subleases of \$1,023,000, \$ 772,000, \$521,000, \$438,000, \$38,000, and \$5,000 for 2002, 2003, 2004, 2005, 2006, and thereafter, respectively. Rental expense was \$ ,000 for the one month period ended January 31, 2002.

**Obligations Under License Agreements**

The Company has entered into license agreements with property owners and/or operators of several office buildings whereby the Company has the right to provide communications services in these buildings. Under the terms of the agreements, the Company is generally obligated to pay a commission based on the greater of a base fee or a percentage of revenue earned in the related building or development. At January 31, 2001, the Company's aggregate minimum obligation under these agreements, assuming a December 31 year-end, were as follows:

|      |              |
|------|--------------|
| 2002 | \$ 1,072,000 |
| 2003 | 1,164,000    |
| 2004 | 1,147,000    |
| 2005 | 539,000      |
| 2006 | 316,000      |

|            |              |
|------------|--------------|
| Thereafter | 862,000      |
|            | \$ 5,100,000 |

The commitments above exclude an estimated total of \$2.4 million of potential obligations under license agreements in buildings in which the Company's communications network has not been constructed. In the opinion of management, such amounts will not be owed as the Company is not providing services in those buildings.

**Table of Contents**

**OBLIGATIONS UNDER COMMUNICATIONS SERVICE AGREEMENTS**

At January 31, 2002, the Company had contracts with several communications providers with minimum purchase obligations for leased voice and data transport, equipment collocation, and other services. As of January 31, 2001, approximate future minimum purchase commitments, assuming a December 31 year-end, under these agreements were as follows:

|            |              |
|------------|--------------|
| 2002       | \$ 1,933,000 |
| 2003       | 309,000      |
| 2004       | 189,000      |
| 2005       | 66,000       |
| 2006       | 4,000        |
| Thereafter | 9,000        |
|            | \$ 2,510,000 |

**LEGAL PROCEEDINGS**

The Company is subject to legal proceedings and claims, including employment and other matters that arise in the ordinary course of business. There are no pending legal proceedings to which the Company is a party that management believes will have a material adverse effect on the financial position, results of operations, or cash flows of the Company.

**4. INCOME TAXES**

The Company has estimated net operating loss carryforwards of approximately \$222 million. The net operating loss carryforwards begin to expire in the year 2017 if not previously utilized. Additionally, use of the Company's net operating losses is limited due to certain ownership changes as defined in Section 382 of the Internal Revenue Code. Utilization of existing net operating loss carryforward may be further limited in future years as a result of the purchase by Cypress Holding (Note 5).

**5. SUBSEQUENT EVENTS**

**ACQUISITION OF THE COMPANY**

In January 2002, the Company entered into a definitive agreement providing for the sale of the Company to Cypress Holding. Pursuant to the agreement, Cypress Holding initiated a tender offer for all the outstanding shares of common stock of the Company, including the associated rights to purchase preferred stock, at \$3.50 per share net to the seller, in cash. The transaction, which was subject to 90% of the shares outstanding being tendered and not withdrawn, as well as other customary and legal closing conditions, was completed on February 25, 2002 with approximately 94% of the shares tendered for cash payments of approximately \$15 million. The acquisition of the remaining shares was completed immediately after the closing of the tender through the short-form merger of a wholly owned subsidiary of Cypress Holding with and into the Company, with Cypress Communications surviving as a wholly owned subsidiary of Cypress Holding.

The merger agreement provided that at the date of closing, each then-outstanding option to purchase shares of Cypress Communications common stock under any option plan, program or arrangement of Cypress Communications

( Option ), whether or not such Option is then exercisable or vested, was converted into an obligation of Cypress Communications to pay to the option holder a cash amount equal to the product of (i) the excess, if any, of the offer price over the applicable per share exercise price of such Option and (ii) the number of shares subject to such Option.

In connection with the merger and resulting change of control, the Company paid out severance of \$400,000 to the Company's former CEO under a severance and separation arrangements that existed at December 31, 2001. Additionally, in February 2002, the Company entered into severance arrangements

**Table of Contents**

with certain other officers and employees of the Company. Under these arrangements, the Company paid out severance of approximately \$400,000 upon the change of control resulting from the acquisition of the Company by Cypress Holding.

**ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE**

None.

**ITEM 9A. CONTROLS AND PROCEDURES**

(a) *Evaluation of disclosure controls and procedures* Pursuant to Rule 13a-15(b) under the Securities Exchange Act of 1934, as amended (the Exchange Act), Cypress Holding carried out an evaluation, with the participation of Cypress Holding's management, including Cypress Holding's Chief Executive Officer and Chief Financial Officer, of the effectiveness of Cypress Holding's disclosure controls and procedures (as defined under Rule 13a-15(e) under the Exchange Act) as of the end of the period covered by this report. Based upon that evaluation, Cypress Holding's Chief Executive Officer and Chief Financial Officer concluded that Cypress Holding's disclosure controls and procedures are effective to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act, is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

(b) *Changes in internal controls* Cypress implemented additional procedures designed to strengthen its existing internal controls that were not previously effective in monitoring Cypress's exempt status for telecommunications taxes and surcharges, as more fully described in Note 9(e) to Cypress's audited consolidated financial statements, there has been no change in Cypress Holding's internal control over financial reporting during the quarter ended December 31, 2004 that has materially affected, or is reasonably likely to materially affect, Cypress Holding's internal control over financial reporting. There were no other changes that are reasonably likely to materially affect, Cypress Holding's internal control over financial reporting.

**ITEM 9B. OTHER INFORMATION**

None.

**Table of Contents****PART III****ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT**

Cypress Holding's executive officers and directors, and their ages are as follows:

| <b>Name</b>          | <b>Age</b> | <b>Position</b>                                                 |
|----------------------|------------|-----------------------------------------------------------------|
| Gregory P. McGraw    | 50         | Chief Executive Officer, President, Secretary and Director      |
| Salvatore W. Collura | 51         | Executive Vice President and Chief Operating Officer            |
| Neal L. Miller       | 45         | Executive Vice President, Chief Financial Officer and Treasurer |
| Michael A. Floyd     | 46         | Senior Vice President and Chief Marketing Officer               |
| Ross J. Mangano      | 59         | Chairman of the Board                                           |
| Gerard H. Sweeney    | 48         | Director                                                        |
| Steve G. Nussrallah  | 54         | Director                                                        |
| Michael F. Elliott   | 46         | Director                                                        |

**Gregory P. McGraw** has served as chief executive officer since May 2004 and as president of Cypress Holding since July 2002. Mr. McGraw also served as acting chief executive officer from March 2004 to May 2004, as chief operating officer from July 2002 to June 2004, as chief financial officer from July 2002 to November 2003 and as executive vice president from April 2002 to July 2002. Mr. McGraw has served as chief executive officer of Cypress Communications since May 2004 and as president of Cypress Communications since February 2002. Mr. McGraw has served as a director of Cypress Holding since June 2004. Mr. McGraw served as president and chief operating officer of Resurgence Communications, LLC from January 2001 to February 2002. Prior to that, he was executive vice president and corporate development officer for Convergent Communications, Inc. from August 1998 to January 2001. From July 1996 to August 1998, Mr. McGraw was a regulatory consultant, vice president of marketing and served as interim chief financial officer for Tie Communications, Inc. Mr. McGraw has a BS in Business Administration from George Mason University in Virginia.

**Salvatore W. Collura** has served as chief operating officer since June 2004 and as executive vice president of Cypress Holding since July 2002. Mr. Collura has served as chief operating officer of Cypress Communications since June 2004 and as executive vice president of Cypress Communications since February 2002. Mr. Collura has more than 25 years of sales and operations management experience in the telecommunications industry and was most recently the executive vice president of Convergent Communications' Voice Division. During his 17 years at Tie Communications, Mr. Collura held various regional and national positions in sales and general management and consistently earned top sales honors and awards. Prior to Tie Communications' acquisition by Convergent, Mr. Collura was a regional VP/GM. Mr. Collura has a BS in Business Administration from the University of Nebraska at Lincoln.

**Neal L. Miller** has served as executive vice president, chief financial officer and treasurer of Cypress Holding and Cypress Communications since November 2003. Mr. Miller has extensive experience building and managing financial business units and leading strategic planning and corporate development programs in the telecommunications, cable and software industries. From March 2003 to October 2003, Mr. Miller was an independent consultant providing financial and operations management expertise to several companies in the cable TV, software and telecom industries. From March 2000 to February 2003, Mr. Miller served as executive vice president and chief financial officer of CES International Inc., a software provider for the electric utility industry. Mr. Miller served as executive vice president and chief financial officer of Syntellect, Inc. from December 1995 to July 1998 and as a division president of Syntellect Interactive Services, Syntellect's hosted services business unit, from February 1998 to February 2000. Mr. Miller has a BBA in Accounting from Georgia State University in Atlanta, Georgia.



**Michael A. Floyd** has served as senior vice president and chief marketing officer of Cypress Communications since June 2004. From August 2003 to May 2004, Mr. Floyd served as an executive consultant for Cypress Communications focused on optimizing the sales channel model and Voice over

## Table of Contents

Internet Protocol (VoIP) initiatives. Mr. Floyd has extensive experience launching and managing new organizations, creating winning business strategies, leading transformational change and developing effective sales channel models in the telecommunications, data network, service provider and software industries. From January 2001 to March 2003, Mr. Floyd served as Senior Partner for Trilogy Software providing executive management consulting and custom software solutions to optimize multi-channel sales organizations. From March 1998 to December 2001, Mr. Floyd served as vice president and general manager of eBusiness for Bellsouth providing managed services, internet solutions, e-commerce solutions, data network infrastructure and call center solutions to Bellsouth business customers. Mr. Floyd has a BS in business administration from the University of North Carolina at Chapel Hill, North Carolina.

**Ross J. Mangano** has served as a director of Cypress Holding since October 1998 and chairman of the board since February 2002. Mr. Mangano has also served as director and chairman of the board of Cypress Communications since February 2002. Mr. Mangano has served as the president of Oliver Estate, Inc., an investment management company located in South Bend, Indiana, since 1996. Prior to that time, Mr. Mangano served in various management positions with Oliver Estate, Inc. since 1971. Mr. Mangano also is an investment analyst for Oliver Estate, Inc. Mr. Mangano has served on the board of directors of BioSante Pharmaceuticals, Inc., a public company located in Lincolnshire, Illinois, since July 1999 and Orchard Software Company, a privately held company which develops software for the medical industry located in Carmel, Indiana, since August 1998.

**Gerard H. Sweeney** has served as a director of Cypress Holding since January 2000 and as a director of Cypress Communications since February 2002. Mr. Sweeney also serves as president, chief executive officer and trustee of Brandywine Realty Trust. Mr. Sweeney has served as chief executive officer of Brandywine since August 1994, as president since November 1988 and as a trustee since February 1994. Brandywine Realty Trust is a public real estate investment trust located in Newtown Square, Pennsylvania. Prior to August 1988, Mr. Sweeney served as vice president of LCOR, Incorporated, a real estate development firm. Mr. Sweeney was employed by the Linpro Company (a predecessor of LCOR) from 1983 to 1994, during which time he served in several capacities, including financial vice president and general partner.

**Steve G. Nussrallah** has served as a director of Cypress Holding and Cypress Communications since July 2002. Mr. Nussrallah has been a general partner of Noro-Moseley Partners, an Atlanta-based venture capital firm, since January 2001. Mr. Nussrallah has also served as chairman of the board of Concurrent Computer Corp., since October 2000. Before becoming chairman, Mr. Nussrallah served as president and chief executive officer of Concurrent from January 2000 to October 2000 and as president of its Xtreme division from January 1999 to December 1999. From March 1996 to March 1998, Mr. Nussrallah served as president and chief operating officer of Syntellect Inc.

**Michael F. Elliott** has served as a director of Cypress Holding and Cypress Communications since July 2002. Mr. Elliott has served as a managing director of Wakefield Group, a North Carolina-based venture capital firm, since March 1997. Mr. Elliott served as a managing director of NationsBank Capital Investors from January 1994 through March 1997 and was a founding General Partner of NCNB Venture Co., LP. Prior to joining NationsBank, Mr. Elliott was a member of Ernst & Young's Corporate Finance Group. Mr. Elliott serves as a director of several of the Wakefield Group's portfolio companies.

**Audit Committee Financial Expert.** The Board of Directors has determined that Gerard H. Sweeney is an audit committee financial expert as such term is defined in the rules promulgated by the SEC under the Sarbanes-Oxley Act of 2002.

## **SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Section 16(a) of the Exchange Act requires Cypress Holding's directors and executive officers, and persons who own more than 10% of Cypress Holding's outstanding common stock, to file with the SEC initial reports of ownership and reports of changes in ownership of common stock. These persons are required by SEC regulation to furnish us with copies of all such reports they file.

**Table of Contents**

To Cypress Holding's knowledge, based solely on a review of Forms 3 and 4 and amendments thereto furnished to Cypress Holding under Exchange Act Rule 16a-3(e) during the year ended December 31, 2003 and Form 5 and amendments thereto furnished to Cypress Holding with respect to the year ended December 31, 2003, and any written representation that a Form 5 is not required to be filed, Cypress Holding believes that all of its directors, executive officers, 10% stockholders and other individuals designated as Section 16 filers by Cypress Holding complied during the year ended December 31, 2004 with the reporting requirements of Section 16(a) of the Exchange Act.

**CODE OF ETHICS**

Cypress Holding has adopted a Code of Ethics for its chief executive officer and senior financial officers. A copy of this code may be found at [www.cypresscom.net](http://www.cypresscom.net). You will find the Code of Ethics by clicking Investors then Corporate Governance. Cypress Holding will satisfy the disclosure requirement under Item 5.05 of Form 8-K by posting such information on its website. The information set forth on this website should not be deemed filed with, and is not incorporated by reference into, this Form 10-K or any of Cypress Holding's other filings under the Securities Act or the Exchange Act, except to the extent that Cypress Holding specifically so provides.

**ITEM 11. EXECUTIVE COMPENSATION**

Summary Compensation Table

The following table sets forth summary information concerning total compensation earned or paid to (i) Cypress Holding's Chief Executive Officer during the year ended December 31, 2004, (ii) the four most highly compensated executive officers who served in such capacities as of December 31, 2004, which includes one executive officer of Cypress Holding's wholly owned subsidiary, Cypress Communications, and (iii) Cypress Holding's former Chief Executive Officer, collectively referred to below as the named executive officers, for the fiscal years ended December 31, 2002, 2003 and 2004:

**Table of Contents**

| Name and Principal Position | Year | Annual Compensation |           | Long Term Compensation Awards Securities |                        | All Other Compensation |
|-----------------------------|------|---------------------|-----------|------------------------------------------|------------------------|------------------------|
|                             |      | Salary              | Bonus     | Other Annual Compensation                | Underlying Options (#) |                        |
| Gregory P. McGraw           | 2004 | \$ 268,750          | \$        | \$                                       | 150,000(1)             |                        |
| Chief Executive Officer,    | 2003 | \$ 300,000          | \$ 37,500 | \$                                       |                        |                        |
| President and Secretary     | 2002 | \$ 230,556          | \$        | \$                                       | 1,100,000(1)           |                        |
| Salvatore W. Collura        | 2004 | \$ 220,000          | \$ 34,022 | \$                                       | 100,000(1)             |                        |
| Executive Vice President    | 2003 | \$ 220,000          | \$ 17,000 | \$                                       | 100,000(1)             |                        |
| and Chief Operating Officer | 2002 | \$ 160,243          | \$        | \$                                       | 150,000(1)             |                        |
| Neal L. Miller              | 2004 | \$ 200,000          | \$ 17,293 | \$                                       | 100,000(1)             |                        |
| Executive Vice President,   | 2003 | \$ 33,333           | \$        | \$                                       | 300,000(1)             |                        |
| Chief Financial Officer and |      |                     |           |                                          |                        |                        |
| Treasurer                   | 2002 | \$                  | \$        | \$                                       |                        |                        |
| Michael A. Floyd            | 2004 | \$ 97,500           | \$ 11,117 | \$                                       | 75,000(1)              |                        |
| Senior Vice President and   | 2003 | \$                  | \$        | \$                                       |                        |                        |
| Chief Marketing Officer     | 2002 | \$                  | \$        | \$                                       |                        |                        |
| Thomas J. Francis           | 2004 | \$ 150,000          | \$ 12,264 | \$                                       | 10,000(1)              |                        |
| Senior Vice President of    | 2003 | \$ 106,250          | \$        | \$                                       | 50,000(1)              |                        |
| Cypress Communications      | 2002 | \$                  | \$        | \$                                       |                        |                        |
| Charles B. McNamee          | 2004 | \$ 62,500           | \$        | \$                                       |                        | \$ 180,000(3)          |
| Former Chief Executive      | 2003 | \$ 300,000          | \$ 37,500 | \$                                       |                        |                        |
| Officer (2)                 | 2002 | \$ 230,556          | \$        | \$                                       | 1,100,000(1)(2)        |                        |

(1) Stock options issued pursuant to 1999 Employee Equity Incentive Plan.

(2) Mr. McNamee left employment with Cypress Holding in March 2004 at which time he forfeited 550,000 unvested options granted in 2002.

(3) Severance.

**Table of Contents****Stock Option Grants in Fiscal 2004**

| Name                 | Number of Securities | % of Total Options/<br>SARS Granted to Employees in Fiscal Year | Exercise or Base Price(\$/Sh) | Expiration Date | Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Term |            |
|----------------------|----------------------|-----------------------------------------------------------------|-------------------------------|-----------------|------------------------------------------------------------------------------------------------|------------|
|                      |                      |                                                                 |                               |                 | 5%(\$)                                                                                         | 10%(\$)    |
| Charles B. McNamee   |                      |                                                                 |                               |                 |                                                                                                |            |
| Gregory P. McGraw    | 150,000 (1)          | 20.65%                                                          | 1.25                          | 4/20/14         | \$ 108,171                                                                                     | \$ 250,524 |
| Salvatore W. Collura | 100,000 (1)          | 13.76%                                                          | 1.25                          | 4/20/14         | 72,114                                                                                         | 167,016    |
| Neal L. Miller       | 100,000 (1)          | 13.76%                                                          | 1.25                          | 4/20/14         | 72,114                                                                                         | 167,016    |
| Michael A. Floyd     | 75,000 (1)           | 10.32%                                                          | 1.25                          | 6/15/14         | 74,840                                                                                         | 142,457    |
| Thomas J. Francis    | 10,000 (1)           | 1.38%                                                           | 1.25                          | 2/2/14          | 6,750                                                                                          | 16,320     |

(1) These incentive stock options vest 25% on each of the first four anniversaries of the grant date.

**Aggregated Stock Option Exercises and Values for Fiscal 2004**

| Name                 | Shares Acquired Upon Exercise | Realized Value | Number of Shares                                   |                                                     | Value of Unexercised in-the-Money Options at Year Ended December 31, 2004 |               |
|----------------------|-------------------------------|----------------|----------------------------------------------------|-----------------------------------------------------|---------------------------------------------------------------------------|---------------|
|                      |                               |                | Underlying Options at Year Ended December 31, 2004 | Unexercised Options at Year Ended December 31, 2004 | Exercisable                                                               | Unexercisable |
| Charles B. McNamee   |                               | \$             | 550,000                                            |                                                     | \$                                                                        | \$            |
| Gregory P. McGraw    |                               | \$             | 825,000                                            | 275,000                                             | \$                                                                        | \$            |
| Salvatore W. Collura |                               | \$             | 100,000                                            | 250,000                                             | \$                                                                        | \$            |
| Neal L. Miller       |                               | \$             | 75,000                                             | 325,000                                             | \$                                                                        | \$            |
| Michael A. Floyd     |                               | \$             |                                                    | 75,000                                              | \$                                                                        | \$            |
| Thomas J. Francis    |                               | \$             | 12,500                                             | 47,500                                              | \$                                                                        | \$            |

**Director Compensation**

All directors are reimbursed for travel expenses incurred in connection with attending board and committee meetings. Directors are not entitled to additional fees for serving on committees of the board. From time to time, the Company may also grant to its non-employee directors options after reviewing the level of compensation paid to non-employee directors by other similarly situated companies.

**Employment Agreements and Retention Awards**

*Charles B. McNamee.* Charles B. McNamee, former chief executive officer of the Company and Cypress Communications, entered into an employment agreement with Cypress Communications in February 2002. The

agreement continued until he left employment with us in March 2004. Pursuant to the agreement, as amended, Mr. McNamee received an annualized salary of \$300,000. Mr. McNamee also received options to purchase 1,100,000 shares of Cypress Holding common stock.

**Table of Contents**

*Gregory P. McGraw.* Gregory P. McGraw, chief executive officer, president and director of Cypress Holding and chief executive officer and president of Cypress Communications, entered into an employment agreement with Cypress Communications in February 2002. This agreement was modified by unanimous written consent of the board of directors in April 2004. The agreement is for a term of one year and will continue year to year unless sooner terminated. Pursuant to the agreement, as amended, Mr. McGraw will serve as the president and chief operating officer of Cypress Communications and will receive an annualized salary of \$250,000. Mr. McGraw is eligible for an executive incentive bonus plan equal to \$100,000.00 upon the completion of 100% of the performance objectives set by the Board for fiscal year 2004. Mr. McGraw also received options to purchase 150,000 shares of Cypress Holding common stock. Under the agreement, Mr. McGraw is eligible to participate in any bonus, incentive, profit-sharing, performance, discretionary pay or similar agreement, plan, policy, program or arrangement adopted by the board of directors. In addition, Mr. McGraw also receives other benefits generally available to Company employees, including paid vacation, insurance benefits and other benefit plans. If Mr. McGraw is terminated without cause or coincident with a change of control or terminates his own employment for good reason (as defined in his agreement), he will continue to receive his base salary and benefits for 12 months following the date of termination and the Company shall accelerate Mr. McGraw's stock options.

*Neal L. Miller.* Neal L. Miller, executive vice president, chief financial officer and treasurer of Cypress Holding and the executive vice president and chief financial officer of Cypress Communications, entered into an employment agreement with Cypress Communications in November 2003. The agreement is for a term of one year and will continue year to year unless sooner terminated. Pursuant to the agreement, Mr. Miller will serve as the executive vice president and chief financial officer of Cypress Communications and will receive an annualized salary of \$200,000. Mr. Miller also received options to purchase 300,000 shares of Cypress Holding common stock. Under the agreement, Mr. Miller is eligible to participate in any bonus, incentive, profit-sharing, performance, discretionary pay or similar agreement, plan, policy, program or arrangement adopted by the board of directors. In addition, Mr. Miller also receives other benefits generally available to Company employees, including paid vacation, insurance benefits and other benefit plans. If Mr. Miller is terminated without cause or coincident with a change of control or terminates his own employment for good reason (as defined in his agreement), he will continue to receive his base salary and benefits for 6 months following the date of termination. In certain termination situations, including a change of control, the Company shall accelerate Mr. Miller's stock options.

*Salvatore W. Collura.* Salvatore W. Collura, executive vice president and chief operating officer of Cypress Holding, entered into an employment agreement with Cypress Holding in May 2004. The agreement is for a term of one year and will continue year to year unless sooner terminated. Pursuant to the agreement Mr. Collura will serve as the executive vice president and chief operating officer of Cypress Holding and will receive an annualized salary of \$220,000. Mr. Collura also received options to purchase 100,000 shares of Cypress Holding common stock. Under the agreement, Mr. Collura is eligible to participate in any bonus, incentive, profit-sharing, performance, discretionary pay or similar agreement, plan, policy, program or arrangement adopted by the board of directors. In addition, Mr. Collura also receives other benefits generally available to Company employees, including paid vacation, insurance benefits and other benefit plans. If Mr. Collura is terminated without cause or coincident with a change of control or terminates his own employment for good reason (as defined in his agreement), he will continue to receive his base salary and benefits for 6 months following the date of termination. In certain termination situations, including a change of control, the Company shall accelerate Mr. Collura's stock options.

*Key Executive Officer Retention Plan.* In connection with our board of directors consideration of a change in control event, the board adopted the Cypress Communications, Inc. Key Executive Officer Retention Plan, or KEORP, in August 2004 and amended the KEORP with respect to the President and Chief Executive Officer in November 2004. The key executive officer participants in the KEORP are Gregory P. McGraw, Salvatore W. Collura and Neal L. Miller. Pursuant to the KEORP, the executive officers were granted retention awards payable following a change in control event if within twelve months of the change of control the executive officer's employment is



terminated without cause or the executive

**Table of Contents**

officer resigns for good reason. In addition, the employment agreement for each of these executive officers includes a severance award, pursuant to which each executive officer would be entitled to receive payment over 6 or 12 months in the event that, coincident with a change in control event, the executive officer's employment is terminated at employee's direction or otherwise. Upon termination in connection with a change in control event, the executive officers are entitled to severance and retention awards as follows:

| <b>Executive Officer</b>                                                        | <b>Severance Award</b> | <b>Retention Award</b> |
|---------------------------------------------------------------------------------|------------------------|------------------------|
| Greg McGraw, President and Chief Executive Officer                              | \$ 300,000             | \$ 375,000             |
| Salvatore W. Collura, Executive Vice-President and Chief Operating Officer      | \$ 110,000             | \$ 100,000             |
| Neal L. Miller, Executive Vice-President, Chief Financial Officer and Treasurer | \$ 100,000             | \$ 100,000             |

## **ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

As of March 1, 2005, we had 6,723,395 issued and outstanding shares of common stock. The following table presents information about the beneficial ownership of our common stock, as of March 1, 2005 by each person or group we know to own more the 5% of the common stock, by each of our directors and executive officers, and by all of our directors and executive officers as a group. The beneficial ownership table includes warrants and options exercisable within 60 days.

| <b>Name of Beneficial Owner</b>                       | <b>Number of Shares Common Stock Beneficially Owned</b> | <b>Percent of Shares of Common Stock Outstanding</b> | <b>Number of Shares Preferred Stock Beneficially Owned</b> | <b>Percent of Shares of Preferred Stock Outstanding</b> |
|-------------------------------------------------------|---------------------------------------------------------|------------------------------------------------------|------------------------------------------------------------|---------------------------------------------------------|
| <i>5% Stockholders</i>                                |                                                         |                                                      |                                                            |                                                         |
| Brandywine Operating Partnership, L.P. <sup>(1)</sup> | 532,692                                                 | 7.75%                                                |                                                            | %                                                       |
| Noro-Moseley V, LLP <sup>(2)</sup>                    | 8,007,390                                               | 54.35%                                               | 72.9                                                       | 72.9%                                                   |
| Wakefield Group III, LLC <sup>(3)</sup>               | 1,834,117                                               | 21.43%                                               | 16.7                                                       | 16.7%                                                   |
| Dolphin Equity Partners <sup>(4)</sup>                | 1,131,930                                               | 14.41%                                               | 10.4                                                       | 10.4%                                                   |
| Jo & Co. <sup>(5)</sup>                               | 1,257,232                                               | 18.70%                                               |                                                            | %                                                       |
| Troon & Co. <sup>(6)</sup>                            | 551,615                                                 | 7.91%                                                |                                                            | %                                                       |
| Jordan E. Glazov <sup>(7)</sup>                       | 667,344                                                 | 9.90%                                                |                                                            | %                                                       |
| Charles B. McNamee <sup>(8)</sup>                     | 550,000                                                 | 7.56%                                                |                                                            | %                                                       |
| <i>Directors and Executive Officers</i>               |                                                         |                                                      |                                                            |                                                         |
| Ross J. Mangano <sup>(9)</sup>                        | 2,766,593                                               | 37.86%                                               |                                                            | %                                                       |
| Gerard H. Sweeney <sup>(10)</sup>                     | 577,692                                                 | 8.38%                                                |                                                            | %                                                       |



**Table of Contents**

| <b>Name of Beneficial Owner</b>                                                        | <b>Number of<br/>Shares<br/>Common<br/>Stock<br/>Beneficially<br/>Owned</b> | <b>Percent<br/>of<br/>Shares<br/>of<br/>Common<br/>Stock<br/>Outstanding</b> | <b>Number of<br/>Shares<br/>Preferred<br/>Stock<br/>Beneficially<br/>Owned</b> | <b>Percent<br/>of<br/>Shares<br/>of<br/>Preferred<br/>Stock<br/>Outstanding</b> |
|----------------------------------------------------------------------------------------|-----------------------------------------------------------------------------|------------------------------------------------------------------------------|--------------------------------------------------------------------------------|---------------------------------------------------------------------------------|
| Steve G. Nussrallah <sup>(11)</sup>                                                    | 8,007,390                                                                   | 54.35%                                                                       |                                                                                | %                                                                               |
| Michael F. Elliott <sup>(12)</sup>                                                     | 1,834,117                                                                   | 21.43%                                                                       |                                                                                | %                                                                               |
| Gregory P. McGraw <sup>(13)</sup>                                                      | 1,137,500                                                                   | 14.47%                                                                       |                                                                                | %                                                                               |
| Salvatore C. Collura <sup>(14)</sup>                                                   | 125,000                                                                     | 1.83%                                                                        |                                                                                | %                                                                               |
| Neal L. Miller <sup>(15)</sup>                                                         | 100,000                                                                     | 1.46%                                                                        |                                                                                | %                                                                               |
| Michael A. Floyd                                                                       |                                                                             |                                                                              |                                                                                |                                                                                 |
| Thomas J. Francis <sup>(16)</sup>                                                      | 27,500                                                                      | 0.40%                                                                        |                                                                                |                                                                                 |
| All Current Directors and Executive Officers as a<br>Group (9 persons) <sup>(17)</sup> | 14,575,792                                                                  | 68.43%                                                                       | 100                                                                            | 100%                                                                            |

- (1) The address of Brandywine Operating Partnership, L.P. is 401 Plymouth Road, Suite 500, Plymouth Meeting, Pennsylvania 19462. Includes 148,077 shares subject to warrants exercisable within 60 days of March 1, 2005.
- (2) The address of Noro-Moseley V, LLP is 9 North Parkway Square, 4200 Northside Parkway, Atlanta, Georgia 30327. Includes 8,007,390 shares subject to warrants exercisable within 60 days of March 1, 2005.
- (3) The address of Wakefield Group III, LLC is 1110 East Morehead Street, Charlotte, North Carolina 28204. Includes 1,834,117 shares subject to warrants exercisable within 60 days of March 1, 2005.
- (4) The address of Dolphin Equity partners is 750 Lexington Avenue, New York, New York 10022. Includes 1,131,930 shares subject to warrants exercisable within 60 days of March 1, 2005.
- (5) The address of Jo & Co. is 112 W. Jefferson Blvd., Suite 613, South Bend, Indiana 46601.
- (6) The address of Troon & Co. is 112 W. Jefferson Blvd., Suite 613, South Bend, Indiana 46601. Includes 247,692 shares subject to warrants exercisable within 60 days of March 1, 2005.
- (7) Includes 15,384 shares subject to warrants exercisable within 60 days of March 1, 2005. The remaining 651,960 shares are held in joint tenancy with Mr. Glazov's wife. Does not include 3,568 shares held by one of Mr. Glazov's sons, 3,568 shares held by another of Mr. Glazov's sons and 2,318 shares held by Mr. Glazov's daughter. Mr. Glazov disclaims beneficial ownership of such shares.
- (8) Includes 550,000 shares subject to options exercisable within 60 days of March 1, 2005.
- (9) Includes 25,000 shares of Cypress common stock subject to warrants exercisable within 60 days of March 1, 2005. Includes 404,652 shares held by trusts of which Mr. Mangano serves as trustee, as follows: Joseph D. Oliver Trust - GO Cunningham Fund (98,288), Joseph D. Oliver Trust - James Oliver II Fund (98,288), Joseph D. Oliver Trust - Joseph D. Oliver, Jr. Fund (98,288), Joseph D. Oliver Trust - Susan C. Oliver Fund (98,288), J. Oliver Cunningham Jr. Revoc Trust (11,500). Also includes the following: warrants to purchase 103,500 shares held by the J. Oliver Cunningham Trust; warrants to purchase 103,500 shares held by the Anne C. McClure Trust; warrants to purchase 103,500 shares held by the Jane C. Warriner Trust; 1,257,232 shares held

by Jo & Co., a corporation for which Mr. Mangano serves as President; 68,973 shares held by James Hart over which Mr. Mangano has voting and/or dispositive control. Also includes 303,923 shares and warrants to purchase 247,692 shares held by Troon & Co.

- (10) Includes 25,000 shares subject to warrants exercisable within 60 days of March 1, 2005. Includes 384,615 shares held by Brandywine Operating Partnership, L.P. and 148,077 shares subject to warrants held by Brandywine Operating Partnership, L.P., of which Mr. Sweeney disclaims any beneficial ownership. Mr. Sweeney is the President and Chief Executive Officer of Brandywine Realty Trust, the general partner of Brandywine Operating Partnership, L.P.
- (11) Includes 8,007,390 shares subject to warrants exercisable within 60 days of March 1, 2005.
- (12) Includes 1,834,117 shares subject to warrants exercisable within 60 days of March 1, 2005.
- (13) Includes 1,137,500 shares subject to options exercisable within 60 days of March 1, 2005.

## **Table of Contents**

- (14) Includes 125,000 shares subject to options exercisable within 60 days of March 1, 2005.
- (15) Includes 100,000 shares subject to options exercisable within 60 days of March 1, 2005.
- (16) Includes 27,500 shares subject to options exercisable within 60 days of March 1, 2005.
- (17) See footnotes (8) through (16) above.

### **Equity Compensation Plans**

For information on our equity compensation plans, see Item 5 and Note 10 to our consolidated financial statements.

## **ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

In July 2002, Cypress Holding, through its wholly owned subsidiary, Cypress Communications, completed the purchase of certain assets of Intermedia Advanced Building Networks, the shared tenant telecommunications services business of WorldCom, Inc ( ABN/STS ). Cypress Holding and Cypress Communications raised \$28 million to finance the acquisition. The \$28 million financing included:

- (i) a \$10 million senior secured revolving credit facility from Silicon Valley Bank (as amended, the Senior Credit Facility );
- (ii) an \$8 million bridge loan (the Bridge Loan ) from the J. Oliver Cunningham Trust (the JOC Trust ), the Anne C. McClure Trust (the ACM Trust ), the Jane C. Warriner Trust (the JCW Trust ), Noro-Moseley Partners V, L.P.( Noro-Mosley ), and the Wakefield Group III, LLC ( Wakefield ) and together with the JOC Trust, the ACM Trust, the JCW Trust and Noro-Mosley, the Bridge Lenders ); and
- (iii) the sale of \$10 million of Fixed Rate Convertible Notes due July 1, 2009 (the Convertible Notes ) to Dolphin Communications, Dolphin Netherlands, Noro-Moseley and Wakefield (collectively, the Purchasers ).

The JOC Trust, the ACM Trust and the JCW Trust are affiliates of certain stockholders of Cypress Holding and of Mr. Mangano. Mr. Michael F. Elliot is the managing director of Wakefield. Mr. Steve G. Nussrallah is the general partner of Noro-Moseley.

The Bridge Loan was obtained by Cypress Holding and Cypress Communications pursuant to a Loan Agreement dated July 16, 2002 among Cypress Holding, Cypress Communications and the Bridge Lenders and was amended on March 24, 2004. The Bridge Loan accrues interest at 14% per annum and matures on (A) the earlier to occur of, if the maturity date of the Senior Credit Facility is extended beyond July 16, 2004, (i) one business day following the maturity, acceleration or termination of the Senior Credit Facility and (ii) July 16, 2005 or (B) the earlier to occur of, if the maturity date of the Senior Credit Facility is not extended beyond July 16, 2004, (i) one business day following the refinancing of the Senior Credit Facility with funds sufficient to satisfy Cypress Holding's obligations to the Bridge Lenders and (ii) July 16, 2005. Each Bridge Lender was entitled to receive an initial loan fee equal to 2.5% of that portion of the Bridge Loan that was funded by such Bridge Lender. Because the Bridge Loan was outstanding 60 days after the closing, Cypress Holding and Cypress Communications became obligated to pay each Bridge Lender an additional loan fee equal to 1.25% of the then outstanding principal balance of such Bridge Lender's share of the Bridge Loan. Because the Bridge Loan was outstanding 90 days after the closing of the Bridge Loan, Cypress Holding and Cypress Communications became obligated subsequent to the end of the quarterly period ended September 30, 2002 to pay each Bridge Lender an additional loan fee equal to 1.25% of the then outstanding principal balance of such Bridge Lender's share of the Bridge Loan. Additionally, as the Bridge Loan was outstanding 120 days after the closing of the Bridge Loan, Cypress Holding and Cypress Communications became obligated to pay to each Bridge

Lender an additional loan fee equal to 1.00% of the then outstanding principal balance of such Bridge Lender's share of the Bridge Loan. The loan fees described above are cumulative and are payable on the earlier to occur of the maturity date of the Bridge Loans or the date on which the Bridge Loans are paid in full. At the closing of the

## **Table of Contents**

Bridge Loan, Cypress Holding issued the Bridge Lenders warrants to purchase an aggregate of 400,000 shares of Cypress Holding's common stock at an exercise price of \$1.13 per share. These warrants are exercisable for a term of 10 years.

The Convertible Notes were issued by Cypress Holding and Cypress Communications pursuant to a Purchase Agreement dated July 16, 2002 among Cypress Holding, Cypress Communications and the Purchasers. The Convertible Notes accrue interest at the rate of 7.5% per annum, compounded quarterly, and payable at maturity of the notes, whether upon their stated maturity of July 1, 2009, or earlier as a result of acceleration in the event of a default or upon redemption of the Convertible Notes. The principal of and accrued interest on the Convertible Notes is convertible into Cypress Holding's common stock at \$1.13 per share. The Convertible Notes are redeemable by Cypress Holding or Cypress Communications at any time by payment of the outstanding principal balance and accrued interest. In the event that the Convertible Notes are redeemed, the Purchasers have been issued warrants which will then be eligible for exercise to purchase the number of shares of common stock of Cypress Holding that the Convertible Notes were convertible into on the redemption date at a conversion price of \$1.13 per share. In connection with the issuance of the Convertible Notes, Cypress Holding, the Purchasers and the Bridge Lenders entered into a registration rights agreement, which provides for the registration of the common stock issuable upon (i) the conversion of the Convertible Notes; (ii) the exercise of the Warrants issued in connection with the Bridge Loan; and (iii) the exercise of the Warrants exercisable upon the redemption of the Convertible Notes.

In connection with the issuance of the Convertible Notes, the Purchasers were issued a total of 100 shares of Cypress Holding's Preferred Stock without additional consideration. The rights of the Preferred Stock are set forth in a Certificate of Designations adopted by the Board of Directors. The holders of a majority of the Preferred Stock are entitled to elect two members of the Board of Directors and the holders of the Preferred Stock are entitled to receive dividends and distributions equal to those payable to the holders of an equivalent number of shares of Cypress Holding's common stock. In addition, Cypress Holding may not, without the prior written consent of holders of a majority of the Preferred Stock, (i) increase or decrease (other than by redemption or conversion) the authorized number of shares of Preferred Stock; (ii) cancel or modify the voting rights of the holders of Preferred Stock; cancel or modify the rights of the holders of Preferred Stock; or (iii) amend, waive, alter, modify or repeal any provision of the Certificate of Incorporation or Bylaws of Cypress Holding, if such amendment, alternation, modification or repeal would adversely affect the Preferred Stock, including the issuance of preferred stock with voting rights senior to or pari passu with the Preferred Stock. The Preferred Stock is redeemable by Cypress Holding in the event that:

- (a) at least 75% of the principal amount of the Convertible Notes is converted into shares of common stock of Cypress Holding;
- (b) at least 75% of the principal amount of the Convertible Notes is redeemed;
- (c) Cypress Holding has submitted an application in good faith to apply for listing on AMEX, NASDAQ or another national exchange to register its securities on such exchange, the average daily trading price per share of the common stock as reported in such application is at least \$4.00 per share, and Cypress Holding subsequently receives a comment from such exchange that its application for listing will not be accepted so long as the Series A Preferred remains outstanding with the voting rights described herein; or
- (d) the outstanding principal and interest on the Convertible Notes are paid in full on the maturity date of the Convertible Notes.

The redemption price for the Preferred Stock is \$0.001 per share.

Cypress Holding believes that all transactions between it and the related parties are on terms no less favorable to us than those terms Cypress Holding could have obtained from unaffiliated third parties.





**Table of Contents****ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

During the years ended December 31, 2004 and 2003, Deloitte & Touche billed Cypress Holding the fees set forth below in connection with services rendered by those firms to Cypress Holding.

|                    | 2004   | 2003   |
|--------------------|--------|--------|
| Audit Fees         | \$ 183 | \$ 190 |
| Audit Related Fees | 35     | 9      |
| Tax Fees           | 53     | 54     |
| All Other Fees     | 0      | 0      |
| Total Fees         | \$ 271 | \$ 253 |

Audit Fees include fees for services performed to comply with generally accepted auditing standards, including the recurring audit of Cypress Holding's financial statements. This category also includes fees for audits provided in connection with statutory filings or services that generally only the principal accountant reasonably can provide to a client, such as procedures related to audit of income tax provisions and related reserves, comfort letters, statutory audits, attest services, consents and assistance with and review of documents filed with the SEC.

Audit-Related Fees include fees associated with assurance and related services that are reasonably related to the performance of the audit or review of Cypress Holding's financial statements. This category includes fees related to assistance in financial due diligence related to mergers and acquisitions, consultations regarding generally accepted accounting principles, reviews and evaluations of the impact of new regulatory pronouncements, general assistance with implementation of the new SEC and Sarbanes-Oxley Act of 2002 requirements and audit services not required by statute or regulation. Audit-related fees also include audits of pension and other employee benefit plans, as well as the review of information systems and general internal controls unrelated to the audit of the financial statements.

Tax fees primarily include fees associated with tax audits, tax compliance, tax consulting, as well as domestic and international tax planning. This category also includes tax planning on mergers and acquisitions, restructurings, as well as other services related to tax disclosure and filing requirements.

All other fees primarily include fees associated with products and services provided by the principal accountant, other than those that are included in audit fees, audit-related fees and tax fees.

None of the fees paid to the independent auditors were approved by the Audit Committee after the services were rendered pursuant to the de minimis exception established by the SEC for the provision of non-audit services.

The Audit Committee has considered whether the provision of services described above under Audit Related Fees, Tax Fees, and All Other Fees is compatible with maintaining the independence of Deloitte & Touche, and has concluded that it is so compatible.

*Pre-Approval Policy*

The Audit Committee Charter provides that the Audit Committee shall pre-approve all audit services and permitted non-audit services (including the fees and terms thereof) to be performed for Cypress Holding by its independent auditors; provided that the Chairman of the Audit Committee may pre-approve all auditing and permitted non-audit services that do not exceed \$25,000 and the Chairman shall report any approval given at the next Audit Committee

meeting. The Audit Committee pre-approved all audit fees in 2004.

**Table of Contents**

**PART IV**

**ITEM 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES**

a) Exhibits

| EXHIBITS | DESCRIPTION                                                                                                                                                                                                                                                                                                              |
|----------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 2.1      | Form of Certificate of Merger (1)                                                                                                                                                                                                                                                                                        |
| 2.2      | Plan and Agreement of Merger (1)                                                                                                                                                                                                                                                                                         |
| 2.3      | Agreement and Plan of Merger, dated January 10, 2002 by and among Cypress Communications, Inc., Cypress Communications Holding Co., Inc. and Cypress Merger Sub, Inc. (2)                                                                                                                                                |
| 2.3.1    | Amendment No. 1 to the Merger Agreement, dated January 17, 2002 (2)                                                                                                                                                                                                                                                      |
| 2.4      | Agreement and Plan of Merger, dated November 5, 2004 by and among Cypress Communications Holding Co., Inc., TechInvest Holding Company, Inc. and TechInvest Acquisition, Inc. (13)                                                                                                                                       |
| 2.4.1    | Amendment No. 1 to Agreement and Plan of Merger, dated February 3, 2005 by and among Cypress Communications Holding Co., Inc., TechInvest Holding Company, Inc. and TechInvest Acquisition, Inc. (15)                                                                                                                    |
| 2.5      | Voting Agreement, dated November 5, 2004 by and among TechInvest Holding Company, Inc. and the preferred stockholders listed therein. (13)                                                                                                                                                                               |
| 2.6      | Voting Agreement, dated November 5, 2004 by and among TechInvest Holding Company, Inc. and the common stockholders listed therein. (13)                                                                                                                                                                                  |
| 3.1      | Certificate of Incorporation (1)                                                                                                                                                                                                                                                                                         |
| 3.1.1    | Amendment to Certificate of Incorporation (11)                                                                                                                                                                                                                                                                           |
| 3.2      | Bylaws (3)                                                                                                                                                                                                                                                                                                               |
| 4.1      | Form of Common Stock Certificate (1)                                                                                                                                                                                                                                                                                     |
| 4.2      | Registration Rights Agreement dated October 2, 1998 (1)                                                                                                                                                                                                                                                                  |
| 4.2.1    | Amendment dated September 24, 1999 to Registration Rights Agreement dated October 2, 1998 (1)                                                                                                                                                                                                                            |
| 4.3      | Registration Rights Agreement, dated July 16, 2002, by and among Cypress Communications Holding Co., Inc. and the purchasers listed therein (12)                                                                                                                                                                         |
| 4.4      | Intercreditor (Subordination) Agreement, dated July 16, 2002, J. Oliver Cunningham Trust dated February 26, 1971, the Anne C. McClure Trust dated February 26, 1971, the Jane C. Warriner Trust dated February 26, 1971, Noro-Moseley Partners V, L.P., Wakefield Group III and the Noteholders signatories thereto (12) |

- 10.1 Employment Agreement dated as of February 21, 2002 between Cypress Communications, Inc. and Gregory P. McGraw (4)
- 10.1.1 Unanimous Written Consent In Lieu of a Special Meeting of the Board of Directors of Cypress Communications Holding Co., Inc. modifying the employment agreement of Gregory P. McGraw, Chief Executive Officer and President (14)
- 10.2 Employment Agreement dated as of November 1, 2003 between Cypress Communications and Neal L. Miller (12)
- 10.3 1999 Employee Equity Incentive Plan (1)
- 10.3.1 First Amendment to Cypress Holding s 1999 Employee Equity Incentive Plan (5)
- 10.3.2 Second Amendment to Cypress Holding s 1999 Employee Equity Incentive Plan (6)
- 10.4 Asset Purchase Agreement dated as of October 18, 2000 between Cypress Holding and Apex Site Management, Inc. (7)
- 10.5 Stock Purchase Agreement dated July 26, 2001 between Cypress Holding and Craig M. Siegler (8)
- 10.6 Amended and Restated Loan and Security Agreement dated March 17, 2004 between Cypress Communications, Inc., Cypress Communications Operating Company, Inc. and Silicon Valley Bank (9)
- 10.7 Asset Purchase Agreement, dated May 31, 2002 by and among Intermedia Communications, Inc., Shared Technologies Fairchild, Inc., Share Technologies Fairchild

**Table of Contents**

| EXHIBITS | DESCRIPTION                                                                                                                                                                                                                                                                                                                                                                  |
|----------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|          | Telcom, Inc., MCI Worldcom Communications, Inc., Worldcom, Inc. and Cypress Communications, Inc. (10)                                                                                                                                                                                                                                                                        |
| 10.8.1   | Amendment No. 1 to Asset Purchase Agreement and Waiver, dated July 17, 2002, by and among Intermedia Communications, Inc., Shared Technologies Fairchild, Inc., Share Technologies Fairchild Telcom, Inc., MCI Worldcom Communications, Inc., Worldcom, Inc. and Cypress Communications, Inc. (10)                                                                           |
| 10.9     | Omnibus Post-Closing Agreement, dated July 17, 2002, by and among Intermedia Communications, Inc., Shared Technologies Fairchild, Inc., Share Technologies Fairchild Telcom, Inc., MCI Worldcom Communications, Inc., Worldcom, Inc. and Cypress Communications, Inc. (10)                                                                                                   |
| 10.10    | Loan Agreement, dated as of July 16, 2002, by and among J. Oliver Cunningham Trust dated February 26, 1971, the Anne C. McClure Trust dated February 26, 1971, the Jane C. Warriner Trust dated February 26, 1971, Noro-Moseley Partners V, L.P., Wakefield Group III, LLC, Cypress Communications Holding Co., Inc. and Cypress Communications, Inc. (12)                   |
| 10.11    | First Amendment to the Loan Agreement, dated March 25, 2004, by and among J. Oliver Cunningham Trust dated February 26, 1971, the Anne C. McClure Trust dated February 26, 1971, the Jane C. Warriner Trust dated February 26, 1971, Noro-Moseley Partners V, L.P., Wakefield Group III, LLC, Cypress Communications Holding Co., Inc. and Cypress Communications, Inc. (12) |
| 10.12    | Purchase Agreement, dated July 16, 2002, by and among Cypress Communications Holding Co., Inc. and the parties listed therein (12)                                                                                                                                                                                                                                           |
| 10.13    | Loan Modification Agreement by and among Cypress Communications, Inc., Cypress Communications Operating Company, Inc. and Silicon Valley Bank, dated July 12, 2004 (9)                                                                                                                                                                                                       |
| 10.14    | Executive Employment Agreement dated as of May 15, 2004 between cypress Communications Holding Co., Inc. and Salvatore W. Collura (11)                                                                                                                                                                                                                                       |
| 10.15    | Key Executive Officer Retention Plan, adopted August 16, 2004 (14)                                                                                                                                                                                                                                                                                                           |
| 10.15.1  | First Amendment to the Key Executive Officer Retention Plan, dated November 4, 2004 (14)                                                                                                                                                                                                                                                                                     |
| 10.16    | Executive Compensation Arrangements *                                                                                                                                                                                                                                                                                                                                        |
| 10.17    | Director Compensation Arrangements *                                                                                                                                                                                                                                                                                                                                         |
| 21.1     | List of Cypress Holding s Subsidiaries (6)                                                                                                                                                                                                                                                                                                                                   |
| 31.1     | Certificate of Gregory P. McGraw, Chief Executive Officer pursuant to Rule 13a-14(a)*                                                                                                                                                                                                                                                                                        |
| 31.2     | Certificate of Neal L. Miller, Executive Vice President and Chief Financial Officer pursuant to Rule 13a-14(a)*                                                                                                                                                                                                                                                              |
| 32.1     |                                                                                                                                                                                                                                                                                                                                                                              |

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Certificate of Gregory P. McGraw, Chief Executive Officer pursuant to 18 U.S.C., Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002 \*

32.2 Certificate of Neal L. Miller, Executive Vice President and Chief Financial Officer pursuant to 18 U.S.C., Section 1350, as adopted pursuant to Section 906 of the Sarbanes Oxley Act of 2002 \*

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\* Filed herewith

- (1) Incorporated by reference to Cypress Holding s Registration Statement on Form 10-SB12G/A filed on June 8, 2000 (Registration No. 000-30401).
- (2) Incorporated by reference to Cypress Holding s Schedule TO filed on January 22, 2002.
- (3) Incorporated by reference to Cypress Holding s Form 10-QSB filed on August 14, 2002.
- (4) Incorporated by reference to Cypress Holding s Form 10-KSB filed April 16, 2002.

83

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**Table of Contents**

- (5) Incorporated by reference to Cypress Holding s Definitive Information Statement on Schedule 14A filed May 21, 2002.
- (6) Incorporated by reference to Cypress Holding s Form 10-KSB filed on April 7, 2003.
- (7) Incorporated by reference to Cypress Holding s Definitive Information Statement on Schedule 14C filed November 7, 2000.
- (8) Incorporated by reference to Cypress Holding s Form 10-QSB filed on November 14, 2001.
- (9) Incorporated by reference to Cypress Holding s Form 8-K filed on July 19, 2004.
- (10) Incorporated by reference to Cypress Holding s Form 8-K filed on July 31, 2002.
- (11) Incorporated by reference to Cypress Holding s Form 10-Q filed on August 10, 2004.
- (12) Incorporated by reference to Cypress Holding s Form 10-KSB filed on March 30, 2004.
- (13) Incorporated by reference to Cypress Holding s Form 8-K filed on November 8, 2004.
- (14) Incorporated by reference to Cypress Holding s Form 10-Q filed on February 4, 2005.
- (15) Incorporated by reference to Cypress Holding s Form 8-K filed on February 7, 2005.



**Table of Contents**

**SIGNATURES**

In accordance with Section 13 or 15(d) of the Exchange Act of 1934, the Company caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on April 15, 2005.

CYPRESS COMMUNICATIONS HOLDING CO., INC.

Dated: April 15, 2005

By: /s/ Gregory P. McGraw

Gregory P. McGraw  
President and Chief Executive Officer

Dated: April 15, 2005

By: /s/ Neal L. Miller

Neal L. Miller  
Executive Vice President and Chief Executive Officer

**POWER OF ATTORNEY**

Each person whose signature appears below on this Annual Report on Form 10-K hereby constitutes and appoints Gregory P. McGraw and Neal L. Miller, and each of them, his true and lawful attorney-in-fact, acting alone, with full powers of substitution and resubstitution, for him and in his name, place and stead, in any and all capacities (until revoked in writing), to sign any or all amendments to this Annual Report on Form 10-K of Cypress Communications Holding Co., Inc., and to file the same, with exhibits thereto, and other documents to be filed in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that said attorney-in-fact or his substitute, acting alone, may lawfully do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed by the following persons in the capacities and on the dates indicated.

| SIGNATURE                      | TITLE                                                      | DATE           |
|--------------------------------|------------------------------------------------------------|----------------|
| /s/ Gregory P. McGraw<br><hr/> | Director, Chief Executive Officer, President and Secretary | April 15, 2005 |
| Gregory P. McGraw              |                                                            |                |
| /s/ Neal L. Miller<br><hr/>    | Executive Vice President and Chief Financial Officer       | April 15, 2005 |
| Neal L. Miller                 |                                                            |                |
| /s/ Ross J. Mangano<br><hr/>   | Director<br>(Non-Executive Chairman of the Board)          | April 15, 2005 |
| Ross J. Mangano                |                                                            |                |
| /s/ Steve G. Nussrallah        | Director                                                   | April 15, 2005 |

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Steve G. Nussrallah

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/s/ Michael F. Elliott      Director

April 15, 2005

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Michael F. Elliott

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/s/ Gerard H. Sweeney      Director

April 15, 2005

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Gerard H. Sweeney