HICKORY TECH CORP
Form 10-K
March 14, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2006

Commission File Number: 0-13721

HICKORY TECH CORPORATION

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

221 East Hickory Street

P.O. Box 3248

Mankato, Minnesota 56002

(Address of principal executive offices and zip code)

Registrant s telephone number, including area code: **800-326-5789**

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

Title of each class	Name of each exchange on which registered
Common Stock, no par value	**The NASDAQ Stock Market, LLC**

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x

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

Indicate by a 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. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See the definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

(Check one): Large accelerated filer o accelerated filer x non-accelerated filer o

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

As of June 30, 2006, the aggregate market value of the common stock held by non-affiliates of the registrant was $87,106,103 based on the last sale price of $7.00 on The NASDAQ Stock Market, LLC.

The total number of shares of the registrant s common stock outstanding as of February 28, 2007: 13,237,645.

Documents Incorporated by Reference: Portions of the registrant s definitive Proxy Statement for the Annual Meeting of Shareholders to be held on May 7, 2007 (Proxy Statement) are incorporated by reference in Part III of this Form 10-K.

INDEX

PART I

CAUTIONARY STATEMENT

The Private Securities Litigation Reform Act of 1995 contains certain safe harbor provisions regarding forward-looking statements. This 2006 Annual Report on Form 10-K and other documents filed by HickoryTech Corporation (HickoryTech, the Company, we, us or our) under the federal securities laws, including Form 10-Q and Form 8-K, and future verbal or written statements by HickoryTech and its management, may include forward-looking statements. These statements may include, without limitation, statements with respect to anticipated future operating and financial performance, growth opportunities and growth rates, acquisition and divestiture opportunities, business strategies, business and competitive outlook and other similar forecasts and statements of expectation. Words such as expects, anticipates, intends, plans, believes, seeks, estimates, projects, will, continues, and should, and variations of these words and similar expressions, are intended to identify these forward-looking statements. Such forward-looking statements are subject to risks and uncertainties that could cause HickoryTech s actual results to differ materially from such statements. Risks and uncertainties include:

- Those identified under Business
- Those identified under Risk Factors
- Those identified under Managements Discussion and Analysis of Financial Condition and Results of Operations
- Technological development and changes in the telecommunications industry
- Changes in price and service competition
- Changes in federal and state regulation and the rules and regulations enacted pursuant to legislation
- Regulatory limits on our ability to change pricing
- Possible changes in demand for our products and services
- Changes in general industry, market conditions, and growth rates
- Changes in interest rates or other general national, regional or local economic conditions
- Governmental and public policy changes
- Changes in accounting policies or practices adopted voluntarily or as required by generally accepted accounting principles, and
- Continued availability of financing in the amounts and or the terms and conditions necessary to support our future business

Due to the uncertainties listed and the fact that any forward-looking statements made by HickoryTech and its management are based on estimates, projections, beliefs and assumptions of management, they are not guarantees of future performance. Except where required by law, HickoryTech disclaims any obligation to update or revise any forward-looking statements based on the occurrence of future events, the receipt of new information or otherwise.

GENERAL INFORMATION

We maintain a website at (http://www.HickoryTech.com) to provide information to the general public, customers, shareholders and potential investors about our products, services, general information about our company, its management, and financial reports and news. Copies of our most recent Annual Report or Form 10-K, our Quarterly Reports on Form 10-Q and other reports filed with the Securities and Exchange

Commission (SEC), can be obtained, free of charge, as soon as reasonably practical after such material is electronically filed, or furnished to the SEC. To obtain this information call our investor relations department at 507-387-3355, or provide an email request through our website, or write a request addressed to:

Investor Relations

HickoryTech Corporation

PO Box 3248

221 East Hickory Street

Mankato, MN 56002-3248

Our Board of Directors has adopted a Code of Ethics that is applicable to all of our directors, the chief executive and chief financial officer, and to employees involved in financial reporting. All employees of the Company have adopted a Code of Conduct and undergone extensive training on this code and on ethics. Our Board of Directors has also adopted written charters for all its committees that comply with the NASDAQ Stock Market, LLC. Copies of the committee charters are available on our website or upon request by contacting our Investor Relations department at 507-387-3355 or by writing the Investor Relations department at the address noted above.

All information contained in this 2006 Annual Report on Form 10-K is electronically filed with the SEC. The SEC maintains an Internet site (http://www.sec.gov) that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC. The public may also read and copy any materials that HickoryTech files with the SEC at the SEC Public Reference Room, located at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330.

Item 1. Business.

GENERAL

HickoryTech is a diversified communications company headquartered in Mankato, Minnesota. HickoryTech has over a 100-year history in the local telephone exchange business. It is operated in two business segments: the Telecom Sector and the Enventis Sector. HickoryTech s core business is its Telecom Sector, which consists of two product lines. The first product line of the Telecom Sector is the operation of three incumbent local exchange carriers (ILEC) and the operation of a competitive local exchange carrier (CLEC), which HickoryTech initiated in 1998, and its associated competitive services of long distance and Internet access. The second product line of the Telecom Sector is National Independent Billing, Inc. (NIBI), which provides data processing services to the telecommunications industry. In December 2003, HickoryTech sold what had been a third product line of the Telecom Sector, which provided wireless telecommunications services to customers in southern Minnesota and its surrounding area, along with an area surrounding Minneapolis/St. Paul. All financial statements and schedules have been restated to reflect wireless operations as discontinued operations.

On December 30, 2005, HickoryTech purchased Enventis Telecom (Enventis). Enventis is a Minnesota-based regional provider of integrated fiber network, Internet Protocol (IP) Telephony, and data services, with 1,500 route miles of fiber network serving more than 300 business customers in over 40 communities in the Upper Midwest. Enventis had formerly been a wholly owned subsidiary of another public corporation.

In December 2006, HickoryTech sold what had been a third business segment (Enterprise Solutions), which provided telephone, data and IP equipment sales and service. All financial statements and schedules have been restated to reflect Enterprise Solutions operations as discontinued operations.

Operating results for NIBI, which had previously been reported in the Information Solutions Sector, have been recasted to be included in the Telecom Sector to consolidate our reporting for similar operations for all years presented. With the addition of Enventis, NIBI became a small proportion of the overall HickoryTech operations, measured on relative revenues, operating income, manpower, strategic growth potential and on several other levels. The primary internal user of NIBI services is the Telecom Sector. NIBI activities are of strategic value to HickoryTech, primarily because of the support services it provides to the Telecom Sector. The goals and objectives, and the way the NIBI product line is run, are closely aligned with that of the Telecom Sector. Due to the previously mentioned reasons, the NIBI product line was combined with the Telecom Sector in 2006 and all comparative results were recasted to conform to the current presentation.

The HickoryTech parent company was incorporated in Minnesota in 1985 and replaced Mankato Citizens Telephone Company (formed in 1898) as the parent company.

The seven current subsidiaries of HickoryTech and the business segments in which they operate are:

TELECOM SECTOR

- Mankato Citizens Telephone Company (MCTC)
- Mid-Communications, Inc. (Mid-Comm)
- Heartland Telecommunications Company of Iowa, Inc. (Heartland)
- Cable Network, Inc. (CNI)
- Crystal Communications, Inc. (Crystal)
- National Independent Billing, Inc. (NIBI)

ENVENTIS SECTOR

- Enventis Telecom, Inc. (Enventis)

HickoryTech and its subsidiaries are engaged in businesses that provide services to their customers for a fee. Many of these services are recurring, and, as a result, backlog orders and seasonality are not significant factors. Working capital requirements for the Telecom Sector include the financing of construction of networks, which consists of switches and cable, data, IP and digital TV. Capital requirements are also needed for maintaining a high amount of fixed assets, capital for software development, paying payroll costs of highly skilled labor, maintaining inventory to service capital projects and network and telephone equipment customers, and providing for the carrying value of trade accounts receivable, which may take several months to collect in the normal course of business. Working capital requirements for the Enventis Sector include the construction of fiber/optical equipment, IP equipment, capital for payroll costs, the carrying value of accounts receivable, work-in-process and inventory.

The materials and supplies that are necessary for the operation of the businesses of HickoryTech and its subsidiaries are available from a variety of sources. All of HickoryTech s central office switches are supplied by Nortel. A majority of HickoryTech s equipment sold in its Enventis Sector are supplied by Cisco. Nortel and Cisco are leading suppliers of communications and data equipment, and HickoryTech s dependence on these brands is not viewed as a significant risk.

ACQUISITION

On December 30, 2005, HickoryTech purchased Enventis from ALLETE, Inc. The purchase price was comprised of $35,500,000 in cash, subject to normal working capital adjustments. Enventis is a transport and enterprise IP telephony sales business which specializes in providing telecommunications and network solutions. In addition to its statewide SONET-based network, Enventis provides innovative IP services that combine voice and data onto a single platform. Since 1997, Enventis has provided network solutions for a broad spectrum of large corporate, non-profit, government and small business clients. Enventis has offices located in Duluth, Plymouth, and Rochester, Minnesota and Sioux Falls, South Dakota.

On December 30, 2005, HickoryTech entered into a $160,000,000 credit agreement with a syndicate of banks, which amended its previous credit facility. The proceeds were used to carryover the outstanding obligations under the previous credit facility, pay fees and expenses associated with the new credit facility, and pay costs associated with the acquisition of Enventis (see Note 3 to the Notes to the Consolidated Financial Statements).

DISPOSITIONS

Effective December 31, 2006, HickoryTech sold Collins Communications Systems Co. Collins to Skyview Capital, LLC Skyview . The selling price was comprised of a $100,000 note and up to $1,650,000 of earn-out payments in exchange for all of the Collins outstanding capital stock. Skyview paid HickoryTech $100,000 in February 2007. The remaining selling price is due in contingent payments payable over the next four years based on financial targets reached by Skyview. The $100,000 mentioned above has been included in the calculation of the net loss mentioned below, while the contingent payments have not been included in the net loss. The agreement also contains a service agreement, whereby Skyview agrees to provide customer support as a subcontractor for HickoryTech s Nortel equipment business. This agreement contains covenants against competition by the new owner in south-central Minnesota. HickoryTech recorded a pre-tax loss on the sale of $3,385,000 ($2,040,000 net of income taxes). The Collins results of operations were formerly reported in the Enterprise Solutions Sector. The consolidated statements of operations for all periods presented have been restated to reflect the Collins operations as discontinued operations (see Note 3 to the Notes to the Consolidated Financial Statements).

On December 15, 2003, HickoryTech sold its wireless business, MSWC, to Western Wireless Corporation (WWC). The consolidated statements of operations for all periods presented have been restated to reflect wireless operations as discontinued operations (see Note 3 to the Notes to the Consolidated Financial Statements).

INDUSTRY SEGMENTS FINANCIAL DATA

Financial information about HickoryTech s industry segments is included on pages 24 to 28 and pages 53 to 55 of this 2006 Annual Report on Form 10-K.

INDUSTRY SEGMENTS

HickoryTech reports the business operations of the ILEC and CLEC and their associated services, and data processing (NIBI) services as a single segment referred to as the Telecom Sector. The results of operations of the Enterprise Solutions Sector are reported as discontinued operations (see Note 3 to the Notes to the Consolidated Financial Statements). The other business segment is the Enventis Sector.

TELECOM SECTOR

HickoryTech s Telecom Sector provides local exchange wireline telephone service, long distance, dial-up and broadband Internet access, and owns and operates fiber optic cable facilities. This Sector includes three ILEC s: MCTC, Mid-Comm and Heartland. MCTC and Mid-Comm provide telephone service in south central Minnesota, specifically Mankato (a regional hub) and eleven rural communities surrounding Mankato. The third ILEC, Heartland, provides telephone service for eleven rural communities in northwest Iowa. In total, there are twenty-three ILEC exchanges within the Telecom Sector.

The Telecom Sector also includes Crystal, a CLEC. Crystal provides local telephone service, long distance, dial-up and broadband Internet access, and digital TV on a competitive basis. Crystal also connects communication networks of interexchange and wireless carriers with the equipment and facilities of end users. Crystal has customers in ten rural communities, encompassing eight exchanges in Minnesota and three communities, encompassing two exchanges in Iowa that are not in HickoryTech s ILEC service areas. Crystal also provides digital TV service in eight Minnesota communities in addition to its telephone services described above. They include St. Peter, initiated in 2001; Waseca in 2004; New Richland, Ellendale and St. Clair in 2005; and Faribault, Lake Crystal and Eagle Lake in 2006, all of which are communities where HickoryTech provides telephone service either as an ILEC or CLEC. In September 2006, the Janesville City Council approved a cable television franchise, which will make digital TV services available to the entire community by the spring of 2007. In October 2006, the City Councils of both Mankato and North Mankato unanimously approved cable television franchise agreements, which will allow HickoryTech to offer digital TV services in those communities and is targeted to begin in the second quarter of 2007.

The Telecom Sector also includes NIBI, which provides data processing and related services, principally for HickoryTech companies, other local exchange telephone companies, CLEC s, interexchange network carriers, wireless companies and cable TV providers. NIBI s principal activity is the provision of monthly batch processing of computerized data for HickoryTech companies as well as non-affiliated companies. Services for telephone company customers include the processing of long distance telephone calls from data sources and telephone switches, the preparation of subscriber telephone bills, customer record keeping and carrier access bills. There are a number of companies engaged in supplying data processing services comparable to those furnished by NIBI. Competition is based primarily on price and service. NIBI has developed an integrated billing and management system called SuiteSolution. SuiteSolution can provide wireline and wireless carriers the individual benefits of a billing platform or a total system solution. SuiteSolution is comparable in the majority of functional elements to similar products/companies providing end user billing services for small to medium-size independent wireline and wireless service providers in North America. Certain features and functionality of SuiteSolution, which are based on Request for Proposal responses, are more highly rated than competing products, while other features and functionality may not be as highly rated as competing products. NIBI counts 18 to 20 companies as its primary competitors in marketing to small to medium-size independent wireline and wireless service providers in North America. SuiteSolution does not utilize uniquely patentable inventions or technological innovations in the construction of the product. Commercially available programming languages are utilized in the development of code that may, based on needs of a prospective user, deliver solutions that are preferred over those of competing products.

HickoryTech also owns and operates fiber optic cable facilities in Minnesota in its Telecom Sector, in addition to its Enventis Sector. These facilities are used to transport interexchange communications as a service to telephone industry customers. HickoryTech s Minnesota ILEC s and CLEC are the primary users of the fiber optic cable facilities in the Telecom Sector. None of the remaining companies in the Telecom Sector experienced major changes in operations during 2006 or 2005, other than the cumulative effect of repeated periodic declines in network access revenues and the gradual erosion of access lines in service, which has reduced the profitability of this Sector.

MCTC derives its principal revenues and income from local services charged to subscribers in its service area, access services charged to interexchange carriers and the operation of a toll tandem-switching center in Mankato, Minnesota. Revenues and income for Mid-Comm are also derived from local service charges in its area of operation and by providing access to long distance services for its subscribers through the toll center in Mankato. Local and interexchange telephone access for the two companies is provided on an integrated basis. The local and interexchange telephone access for both telephone companies utilize the same facilities and equipment and are managed and maintained by a common workforce. Heartland derives its principal revenues and income from local services charged to subscribers in its service area in Iowa, as well as from providing interexchange access for its subscribers. Interexchange telephone access is provided by all three of HickoryTech s ILEC subsidiaries by connecting the communications networks of interexchange and wireless carriers with the equipment and facilities of end users through its switched networks or private lines. Network access revenue accounted for 22.5%, 42.8% and 44.9% of total revenue for HickoryTech in 2006, 2005 and 2004 respectively. The lower percentage in 2006 is primarily due to the Enventis acquisition. Without the Enventis Sector, access revenues would have accounted for 39.8% of the total revenue for HickoryTech in 2006.

MCTC and Mid-Comm are Minnesota public utilities operating pursuant to indeterminate permits issued by the Minnesota Public Utilities Commission (MPUC). Heartland is also a public utility, which operates pursuant to a certificate of public convenience and necessity issued by the Iowa Utilities Board (IUB). These state agencies regulate the services provided by MCTC, Mid-Comm and Heartland. CNI operations are not subject to regulation by the state regulatory authority. Neither the MPUC nor the IUB regulate the rate of return or profits of each of HickoryTech s ILEC operations due to the size of these companies relative to state regulation. In Minnesota, regulators monitor MCTC and Mid-Comm price and service levels. MCTC and Mid-Comm local service rates are below those of most Minnesota ILEC s. HickoryTech and its subsidiaries can change its local rates by evaluating various factors, including economic and competitive circumstances.

As local exchange telephone companies, MCTC, Mid-Comm and Heartland provide end office switching and dedicated circuits to long distance interexchange carriers. These relationships allow HickoryTech s telephone subscribers to place long distance telephone calls to the telephone network. HickoryTech provides interexchange access to its network for interexchange carriers to conduct long distance business with individual customers who select a long distance carrier and for termination of calls to all customers. This interexchange access business is separate and distinct from HickoryTech s own long distance retail business, which is operated in its Crystal subsidiary. The long distance interexchange carriers are significant customers of HickoryTech, but no carrier represents more than ten percent of HickoryTech s consolidated revenues.

Alternatives to HickoryTech service include customers leasing private lines in lieu of switched voice services and data services in or adjacent to the territories served by HickoryTech, which permits the bypassing of local telephone switching facilities. Additionally, services provided by other companies utilizing various Internet, wireline or wireless technologies permit bypass of the local exchange network. Cable TV companies also provide Internet, Digital Subscriber Line (DSL) and voice services in our markets. These alternatives to the local exchange service represent a potential threat to HickoryTech s long-term ability to provide local exchange service at economical rates.

Competition exists in several of HickoryTech s ILEC service areas. A municipality has overbuilt Heartland s network in one community in Iowa and now serves over half of that market. Additionally, cable TV providers are offering voice services in several Heartland communities, two Mid-Comm communities and are also poised to do so in additional exchanges, including Mankato. MCTC, Mid-Comm, Heartland and Crystal are also periodically engaged in negotiations or renegotiations of arrangements for network interconnections and potential unit price declines with other wireline carriers and various wireless service providers. Although competition from these various sources may result in reduced revenue, HickoryTech cannot, at this time, estimate the potential impact related to these events or negotiations.

Competition also exists for some of the HickoryTech services provided to interexchange carriers, such as dedicated private lines, network switching and network routing. This competition comes primarily from the interexchange carriers themselves, in that carriers may decide that the services provided by HickoryTech may be redirected or handled on their own network or on other networks. The provision of these services is primarily month-to-month service ordered from a general tariff, which is a schedule of terms, rates and conditions that is approved by the appropriate state or federal agency. The interexchange carriers primarily control the procurement of these services. As interexchange carriers make these service decisions, they have the potential to reduce the Company s revenue in the Telecom Sector. Other services, such as the provision of broadband, long distance service, directory advertising, end user equipment and customer billing services are open to competition.

Crystal began operations in January 1998 as a new CLEC. Crystal offers local service, long distance, dial-up and broadband Internet access services, and digital TV on a competitive basis to customers in southern Minnesota and Iowa, which were not previously served by HickoryTech s Telecom Sector service area. These service offerings provide customers alternatives to the incumbent communication providers in various communities and are offered under the brand name HickoryTech. These services are currently being offered to customers in ten rural communities, encompassing eight exchanges in Minnesota, as well as three communities, encompassing two exchanges in Iowa. Crystal has also been granted the necessary authority to provide service in another ILEC community in Northwest Iowa. Crystal also provides the long distance service, dial-up and broadband Internet access services to HickoryTech s ILEC subscribers and is providing digital TV in one community served by Mid-Comm, as well as seven CLEC communities.

CLEC activities require Crystal to file for authority to operate with the appropriate public utilities commission (PUC) in each state it serves. Crystal competes directly against existing ILEC s in the areas in which it operates. Crystal competes directly with incumbent cable TV providers and satellite for its high speed internet and digital TV services. Crystal is presently providing these services under franchise agreements with local communities. Crystal is not dependent upon any single customer or small group of customers. No single customer in Crystal accounts for ten percent or more of HickoryTech s consolidated revenues.

HickoryTech is investigating a potential civil dispute being discussed with a municipality regarding contract payments from HickoryTech to the municipality in support of the Company s CLEC product line. While no formal dispute or claim has been filed, HickoryTech and the municipality have exchanged letters outlining their disagreement. No estimate of the impact, if any, related to this item can be made by the Company at this time.

7

ENVENTIS SECTOR

On December 30, 2005, HickoryTech acquired Enventis. Through Enventis, HickoryTech provides integrated data services, offering fiber optic-based communication and advanced data services to business communities in the Upper Midwest. Enventis owns or has long-term leases to approximately 1,500 route miles of fiber optic cable. Enventis also has extensive local fiber optic rings that directly connect the Enventis network with its larger clients (e.g. health care, government and education). Other local fiber rings connect the Enventis network to the local telephone company s central offices. This allows Enventis to utilize the telephone company s connections to access its smaller clients. Enventis serves customers through facilities that are primarily leased from third parties. Enventis has business relationships with Cisco Systems, Inc. and is recognized by Cisco as a Gold Partner. The relationship with Cisco Systems, Inc. is a strategic partnership of Cisco (as the supplier) and HickoryTech (as the distributor). Enventis is a regional leader in deploying leading edge technologies such as IP call centers. Enventis has offices located in Plymouth, Duluth and Rochester, Minnesota and Sioux Falls, South Dakota. Enventis provides converged IP services that allow all communications (e.g. voice, video and data) to use the same fiber optic-based delivery technology.

Enventis product portfolio includes Encompass Unified Communications (Encompass), which serves small-to-medium-sized businesses. Encompass is a hosted or managed IP communications service including local and long distance voice; business IP telephony via hosted IP private branch exchange; unified messaging (a single inbox for voicemail, e-mail, and fax), and dedicated Internet access. Encompass leverages Voice over Internet Protocol (VoIP) or IP telephony over a private connection, minimizing upfront capital investment and information technology management overhead. VoIP enables advanced functionality, voice interoperability with PCs, and scalability. Enventis has been granted authority to operate from the PUCs in Minnesota and Wisconsin for private line services that are subject to minimal regulation. Enventis has been granted Minnesota authority to provide regulated local telephone (voice) services. Those services are provided primarily in a fashion that augments its VoIP service. Services provided by Enventis compete directly with those from ILEC s and other providers in the area in which it operates. Enventis is not dependent upon any single customer or small group of customers.

ENTERPRISE SOLUTIONS SECTOR

Effective December 31, 2006, HickoryTech sold Collins to Skyview. The selling price was comprised of a $100,000 note and up to $1,650,000 of earn-out payments in exchange for all of the Collins outstanding capital stock. Skyview paid HickoryTech $100,000 in February 2007. The remaining selling price is due in contingent payments payable over the next four years based on financial targets reached by Skyview. The $100,000 mentioned above has been included in the calculation of the net loss mentioned below, while the contingent payments have not been included in the net loss. The agreement also contains a service agreement, whereby Skyview agrees to provide customer support as a subcontractor for HickoryTech s Nortel equipment business. This agreement contains covenants against competition by the new owner in south-central Minnesota. HickoryTech recorded a pre-tax loss on the sale of $3,385,000 ($2,040,000 net of income taxes). The Collins results of operations were formerly reported in the Enterprise Solutions Sector. The consolidated statements of operations for all periods presented have been restated to reflect the Collins operations as discontinued operations (see Note 3 to the Notes to the Consolidated Financial Statements).

EMPLOYEES

We employ approximately 400 employees most of whom are based in Minnesota. A total of approximately 283 employees are located at our headquarters in Mankato, MN. We have a collective bargaining agreement with the International Brotherhood of Electrical Workers, or IBEW, which covers approximately 93 of our employees and expires in March 2007. Negotiations for this agreement are currently in progress. There have been no work stoppages or strikes by our IBEW employees in the past 30 years and we consider our labor relations to be good.

INTELLECTUAL PROPERTY

We believe we have trademarks, trade names and licenses that are necessary for the operation of our business as we currently conduct it. The HickoryTech logo is a registered trademark of the United States. We do not consider our trademarks, trade names or licenses to be material to the operation of our business.

OTHER REGULATION

The effects of telecommunications regulation on the Company s business is discussed in the business sector discussion above. HickoryTech does not anticipate any material effects on its earnings, capital expenditures or competitive position because of laws pertaining to the protection of the environment.

OTHER COMPETITION

The effects of telecommunications regulation on the Company s business is discussed in the business sector discussion above. HickoryTech s business strategy has been to position itself as a quality communications services provider. Long-term business relationships with its customers have strengthened HickoryTech s business position. HickoryTech believes that its customers value the fact that it is the local company whose goal is to meet the customers communications needs. HickoryTech has several competitive advantages: price, service, investment in technology; direct billing relationship with almost all of the customers in its service territories and is positioned to offer a wide range of wired communications service from one source.

As an integrated communications and equipment service provider to businesses through its Enventis Sector, HickoryTech differentiates itself from competition with its unique affiliation with an operating telecom company, strategic network and its ability to respond quickly.

The long-range effect of competition on the provision of communications services and equipment will depend on technological advances, regulatory actions at both state and federal levels, court decisions, and possible additional future state and federal legislation. The trend resulting from past legislation has been to expand competition in the telecommunications industry. It is imperative to HickoryTech that competition in this industry be fostered with equal amounts of responsibility, regulation and opportunity for all providers.

Item 1A. Risk Factors.

Our business faces many risks, all of which may not be described below. Additional risks of which we are currently unaware or believe to be immaterial may also result in events that could impair our business operations. If any of the events or circumstances described in the following risks actually occur our business, financial condition or results of operations may suffer, and the trading price of our stock could decline.

Risk related to Our Business

A lack of parity between us and our competitors concerning regulatory fees and assessments and tax laws could adversely impact our ability to profitably compete. The telecommunications industry is heavily taxed and assessed. As regulated entities, we serve as the pass-through entity responsible for charging and collecting the fees and taxes from our end-user customers and remitting the monies collected to the taxing and regulatory authorities. Unless regulators and taxing authorities change or clarify their rules and regulations to include our competitors, or deregulate and exclude us, the lack of parity could adversely impact our ability to effectively compete on price.

Consolidation among our customers could result in our losing a customer or experiencing a slowdown as integration takes place. Consolidation may impact our business as our customers focus on integrating their operations. We believe that in certain instances customers engaged in integrating large-scale acquisitions may scale back their purchases of network equipment and network services while the integration is ongoing. Further, once consolidation occurs, our customers may choose to reduce the number of vendors they use to source their equipment or consolidate their circuits or network routing. After a consolidation occurs, there can be no assurance that we will continue to supply equipment or network services to the surviving communications service provider. The impact of significant mergers on our business is likely to be unclear until sometime after such transactions have closed.

Many of our competitors are major communications companies that have more extensive resources. We compete in our various markets with regional telephone companies and cable companies, with large-scale network providers, and all the wireless, Internet and long distance competitors. Many of these companies have substantially greater financial and marketing resources as well as greater name recognition than ours. In addition, given their financial resources and scale, these companies may be able to devote more capital to newer technologies and/or use their cost advantages to reduce prices for an extended period of time.

Shifts in our product mix may result in declines in operating profitability. Possible changes in the demand for our products and services including lower-than-anticipated-demand for telephone services, reductions in access lines per household or minutes of use volume associated with telephone service, declines in demand for data processing services or billing systems for NIBI, in communication and data equipment for the Telecom and the Enventis Sectors, migration in technology from circuit switched to IP based technology for services for all Sectors, and for network solutions for our Telecom and Enventis Sectors, may result in lower operating profitability. In addition, our operating profitability could decrease based on the amount of new products we sell that have lower startup operating profitability than our existing products and services. All of these factors could reduce our operating profitability. Changes in product mix may also cause some of our inventory to become obsolete. We currently manage potential obsolescence through reserves, but future technology changes may exceed current reserves.

Technological advances in the telecommunications industry create increased operating costs. The telecommunications industry has seen ever increasing technological advances over the past several years. These technological advances increase costs to maintain and improve networks and provided top-end communication products and services that are demanded by our customer base in order to stay competitive with other companies that offer similar services. Innovation in the IP network migration of switched communication services as well as in our communication system products may create challenges to our ability to provide high-quality service and may create reduced demand as customers wait to study their choices. Wireless communications, mobile/non-fixed point service and various Internet and satellite communication innovations also create technological competition for us.

The telecommunications industry is highly competitive. The Telecommunications Act of 1996 permitted competition among communication companies for the rights to interconnect with established networks and to establish new networks in order to offer telephone service to customers in a franchised area. We serve as an ILEC in a number of franchised areas, as well as competing in a number of markets against other established incumbents. The differentiating competitive factors include products and service, technology advancement, reputation and price. Competition has increased in many of the markets that we serve and encompasses a majority of the lines serviced in those markets. This enhances the risk that we may not be able to respond on a timely or profitable basis. In addition, other telecommunication carriers look to stay competitive by altering their choice of networking routes, points of interconnection, technology or signaling protocol, and other telecommunication issues, all which could have a material adverse affect on our profitability.

We depend on third parties, over whom we have no control, to deliver our services. Because of the interconnected nature of the communications industry, we depend heavily on other telecommunications companies, network providers, program service providers, and equipment vendors, to deliver our services. In addition, we are dependent on easements, franchises, and licenses from various private and public entities in order to construct and to operate our networks. The failure to maintain in effect the necessary third party arrangements on acceptable terms would have an adverse effect on our ability to conduct our business.

We expect to continue to face significant competition in all parts of our business and the level of competition is expected to intensify. The Telecommunications industry is highly competitive, as explained in the previous section. We may not be able to successfully anticipate and respond to various competitive factors affecting our industry, including regulatory and technology changes that may affect our competitors and us differently, changes in consumer and commercial preferences, demographic trends and discount pricing strategies by our competitors. We also now face competition from cable TV companies, who are providing Internet, DSL and voice services in our markets.

10

We may be nearing the end of the growth phase of our CLEC edge-out strategy initiated in 1998, as the additions for market share penetration in CLEC communities is surpassed by competition and customer churn. We have experienced a slight decline in our CLEC customer base. We have reached a level of penetration in the majority of our CLEC communities where competition and other communication alternatives have increased our customer churn. This enhances the risk that we may experience a future erosion of our customer base in our CLEC markets.

We may not be able to successfully introduce new products and services. Our success depends upon our ability to successfully introduce new products and services, our ability to offer bundled service packages on terms attractive to our customers, our ability to successfully expand our long distance, Internet, and digital TV offerings to new markets, our ability to introduce and distribute the equipment and systems of manufacturers of switching equipment and the suppliers of communications technology compared to the competitive alternatives of other suppliers, the ability of Enventis to provide transport solutions and competitive IP services, including telecommunications and network solutions, and the ability of our CLEC business to provide competitive local service in new markets

We may not accurately predict technological trends or the success of new products in these markets. New product development often requires long-term forecasting of market trends, development and implementation of new technologies and processes and substantial capital investment. In addition, we do not know whether our products and services will meet with market acceptance or be profitable. Many of our competitors have greater resources than we do. If we fail to anticipate or respond in a cost-effective and timely manner to technological developments, changes in industry standards or customer requirements, if we have any significant delays in product development or introduction, or if any of our relationships with our vendors are negatively impacted, our business, operating results and financial condition could be materially adversely affected.

We operate our network and our business under contracts and franchises that are subject to non-renewal or termination. Our network operates pursuant to franchises, permits or rights from public and private entities, which are terminable if we fail to comply with material terms of the authority we receive. These permits, and many contracts we utilize in our network, have fixed terms and must be renewed periodically. Our success is dependent on continuing these relationships without material increase in our expenses or restrictions on our use.

Risk related to the Management of Our Operations

*A failure in our operational systems or infrastructure could impair our liquidity, disrupt our business, damage our reputation and cause los*s. Shortcomings or failures in our internal processes, people or systems could impair our liquidity, disrupt our business, result in liability to customers or regulatory intervention, damage our reputation or result in financial loss. For example, our telephone operations rely on a central switch to complete local and long distance phone calls to various customers. An interruption in the switch operations could lead to interrupted service for customers. To be successful, we will need to continue providing our customers within a high capacity, reliable and secure network. Disruptions or system failures may cause interruptions in service or reduced capacity for customers. In addition, our financial, accounting, data processing or other operating systems and facilities may fail to operate properly or become disabled as a result of events that are wholly or partially beyond our control, thereby adversely affecting our ability to process transactions. Our inability to accommodate an increasing volume of transactions also could constrain our ability to increase revenues and expand our businesses. Despite the existence of contingency plans and facilities, our ability to conduct business may be adversely impacted by a disruption in the infrastructure that supports our businesses and the communities in which these businesses are located.

Employee misconduct is difficult to detect and prevent, and may have an adverse effect on the Company s business. Although we have not experienced any significant employee misconduct to date, there have been a number of highly publicized cases with other companies involving fraud or other misconduct by employees in recent years, and we may run the risk that employee misconduct could occur. It is not always possible to deter or prevent employee misconduct and the precautions that we take to prevent and detect this activity may not be effective in all cases.

Our businesses may be adversely affected if we are unable to hire and retain qualified employees. Our performance is largely dependant on the talents and efforts of highly skilled individuals in the operations of our telecommunication businesses, including telephone operations, billing software development and telecommunications equipment sales and service. Technological advances force our employees to upgrade their knowledge base continually in order to keep pace with these advances. Our ability to compete effectively depends upon our ability to attract new qualified employees and retain and motivate our existing employees. In addition, we may acquire additional businesses in the future and our success will depend, in part, upon our ability to retain and integrate personnel from acquired businesses who are necessary to the continued success or the successful integration of these acquired businesses.

Our operations have undergone material changes, and our actual operating results can be expected to differ from the results indicated in our historical financial statements. As a result of our 2005 acquisition of Enventis, our mix of operating results differs from the operations upon which our historical financial statements are based. Our mix of operating assets is different. Consequently, our historical financial statements may not be reliable as an indicator of future results.

*Unanticipated increases in capital spending, operating or administrative costs, or the impact of new business opportunities requiring significant up-front investments***.** We operate in cash-flow-dependent businesses. Our existing networks require large capitalized up-front investments for growth and maintenance. Our operating expenses in the form of payroll for a highly trained workforce and the maintenance cost of telecommunications networks are also large uses of cash. Our debt service obligation and our dividends to shareholders also require significant cash each year. New business development may require additional up-front investment in assets and funding of early stage operating losses. We have business plans which provide adequate sources of cash from operations to fund these endeavors, and we select the balance of old and new business to appropriately fund the Company. The risk is from any sudden unanticipated increases in cash outflow after we have already initiated our business plans. If this were to happen, we would have to alter our future business plans, which possibly could affect our growth.

We may not be able to manage our growth effectively. Our ability to manage our growth effectively, including our ability to integrate the operations of new businesses internally developed or external businesses acquired into our operations, may adversely affect our business results of operations and financial condition. In addition, our ability to achieve projected economies of scale and cost savings, meet cash flow projections in valuing newly acquired businesses, successfully absorb the impact of changes in accounting policies as required by generally accepted accounting principles, manage the working capital needs of our business and generate cash flow to service our debt, conform with existing debt covenants and negotiate new debt facilities, and identify future acquisition opportunities for growth may also adversely affect our business results of operations and financial condition.

Risk related to Regulations

As an ILEC in our service area, we are subject to regulation that is not applicable to our competitors. Federal regulations require us to, among other things, share facilities, allow unbundled access to our network and resale of our services purchased at wholesale rates, file tariffs for network access charges, maintain certain accounting records, and file certain regulatory reports. As our business becomes increasingly competitive, these regulatory disparities could impede our ILEC business s ability to compete in the marketplace, which, in turn, could have a material adverse effect on our business.

Future regulation may result in lower revenues. The outcome of future regulatory and judicial proceedings pertaining to interconnection agreements and access charge reform may result in greater-than-anticipated reductions in revenues received from federal and state access charges for switching long distance traffic. Regulatory rules and policies also may adversely affect our ability to change our prices for telephone services in response to competitive pressures.

Changes to laws and regulations to which we are subject, and the introduction of new technologies, may result in reduction of revenues from network access charges. Access charges, which are intended to compensate us for originating, terminating or transporting other carriers calls on our network, accounted for approximately 23% of our total revenue in 2006. The large national carriers who pay these charges have advocated in the past, that access charges they are required to pay should be reduced. And some network providers have argued that access charges do not apply to specific types of their traffic. Emerging technologies, such as VoIP, has caused a debate about whether access charges apply. As our business becomes increasingly competitive, the regulatory disparities regarding network access revenue, the marketplace forces on its pricing levels, and our ability to enforce the historical rules for collecting these revenues, could have a material adverse effect on our business. We cannot predict whether or when action may be taken on any of these issues, or what effect any action may have on revenues and costs of our ILEC and CLEC operations.

Risk related to Financial Aspects of Our Company

A failure to maintain effective internal controls could adversely affect our business. Although we have completed the documentation and testing of the effectiveness of our internal control over financial reporting for fiscal 2006, as required by Section 404 of the Sarbanes-Oxley Act of 2002, we expect we will have to incur continuing costs, including increased accounting fees and increased staffing levels, in order to maintain compliance with that section of the Sarbanes-Oxley Act. In addition, our ability to integrate the operations of other companies that we acquire in the future could impact our compliance with Section 404. In the future, if we fail to complete the Sarbanes-Oxley 404 evaluation in a timely manner, or if our independent registered public accounting firm cannot attest in a timely manner to our evaluation or to the efficacy of our internal controls, we could be subject to regulatory scrutiny and a loss of public confidence in our internal controls. In addition, any failure to implement required new or improved controls, or difficulties encountered in their implementation, could harm our operating results or cause us to fail to meet our reporting obligations.

Anti-takeover provisions in our charter documents, our shareholder rights plan and Minnesota law could prevent or delay a change in control of our Company. Provisions of our articles of incorporation and bylaws, our shareholder rights plan (also known as a poison pill) and Minnesota law may discourage, delay or prevent a merger or acquisition that a shareholder may consider favorable and may limit the market price for our common stock. These provisions include the following:

- advance notice requirements for shareholder proposals;
- authorization for our Board of Directors to issue preferred stock without shareholder approval; and
- limitations on business combinations with interested shareholders.

Some of these provisions may discourage a future acquisition of HickoryTech even though our shareholders would receive an attractive value for their shares or a significant number of our shareholders believe such a proposed transaction would be in their best interest.

Customer payment defaults could have an adverse effect on our financial condition and results of operations. As a result of adverse market conditions, some of our customers may experience serious financial difficulties. Some of the interexchange carriers and long distance companies which utilize our network are our largest customers when it comes to recurring revenue. In some cases these difficulties have resulted or may result in bankruptcy filings or cessation of operations. If customers experiencing financial problems default on paying amounts owed to us, we may not be able to collect these amounts or recognize expected revenue. It is possible those customers from whom we expect to derive substantial revenue will default or that the level of defaults will increase. Any material payment defaults by our customers would have an adverse effect on our results of operations and financial condition. We currently manage this exposure through an allowance for doubtful accounts. An unexpected bankruptcy or default from a customer may not be fully reserved in our allowance. In addition, some of our competitors engage in financing transactions with some of their customers for the purchase of equipment. To remain competitive, it may become necessary for us to offer similar financing arrangements. If such financings occur, it would be our intent to sell all or a portion of these commitments and outstanding receivables to third parties. In the past, we have sold some receivables with recourse and have had to compensate the purchaser for the related losses.

13

If we seek to secure additional financing, we may not be able to obtain it. Also, if we are able to secure additional financing, our shareholders may experience dilution of their ownership interest or we may be subject to limitations on our operations. We currently anticipate that our available cash resources, which include our credit facility, existing cash, cash equivalents and available-for sale securities, will be sufficient to meet our anticipated needs for working capital and capital expenditures to execute our near-term business plan, based on current business operations and economic conditions. If our estimates are incorrect and we are unable to generate sufficient cash flows from operations and we expend our credit facility, we may need to raise additional funds. In addition, if one or more of our strategic acquisition opportunities exceeds our existing resources, we may be required to seek additional capital. If we raise additional funds through the issuance of equity or equity-related securities, our shareholders may experience dilution of their ownership interests and the newly issued securities may have rights superior to those of common stock. Our existing debt covenants require a portion of the proceeds of an equity offering be applied to the outstanding debt balance. If we raise additional funds by issuing additional debt, we may be subject to restrictive covenants that could limit our operating flexibility and interest payments could dilute earnings per share.

Our indebtedness could restrict our operations. As of December 31, 2006, we had $143,089,000 of total indebtedness, including current maturities. We refinanced our indebtedness in December 2005. Our indebtedness could restrict our operations because we will use a substantial portion of our cash flow from operations to pay principal and interest on our indebtedness, which will reduce funds available for working capital, capital expenditures, acquisitions and other general corporate purposes.

Our stock price is volatile. Based on the trading history of our common stock and the nature of the market for publicly traded securities of companies in our industry, we believe that some factors have caused and are likely to continue to cause the market price of our common stock to fluctuate substantially. These fluctuations could occur day-to-day or over a longer period of time and mat be accentuated by the lack of liquidity in our stock. The factors that may cause such fluctuations include, without limitation:

- announcements of new products and services by us or our competitors;
- quarterly fluctuations in our financial results or the financial results of our competitors or customers;
- increased competition with our competitors or among our customers;
- consolidation among our competitors or customers;
- disputes concerning intellectual property rights;
- the financial health of HickoryTech, our competitors or our customers;
- developments in telecommunications regulations;
- general economic conditions in the United States or internationally; and
- rumors or speculation regarding HickoryTech s future business results and actions.

In addition, stocks of companies in our industry in the past have experienced significant price and volume fluctuations that are often unrelated to the operating performance of such companies. This market volatility may adversely affect the market price of our common stock.

We are subject to risks associated with changes in interest rates. We face market risks from changes in interest rates. Market fluctuations could affect our results of operations and financial condition adversely. At times, we reduce this risk through the use of derivative financial instruments. However, we do not enter into derivative instruments for the purpose of speculation. We have entered into these interest rate protection agreements, which have remaining maturities of eighteen months, in order to manage our exposure to interest rate movements. If interest rates fail to rise as anticipated when the instruments were acquired, the affect on the Company will be that it will experience higher-than-market-rate interest expense, and have paid for protection which wasn t needed. We also risk entering a higher interest rate environment when the interest rate protection agreements expire in 2008. This could affect our future interest expense level.

We may encounter litigation that has a material impact on our business. We are a party to various lawsuits, proceedings and claims arising in the ordinary course of business or otherwise. Many of these disputes may be resolved amicably without resort to formal litigation. The amount of monetary liability resulting from the ultimate resolution of these matters cannot be determined at this time. None of the matters we are aware of have required us to record loss reserves, and at this time we believe the ultimate resolution of these lawsuits, proceedings and claims will not have a material adverse impact on our business, results of operations or financial condition. Because of the uncertainty inherent in litigation, it is possible that unfavorable resolutions of these or other lawsuits, proceedings and claims against us have a material adverse affect on our business, results of operations or financial condition.

Item 1B. Unresolved Staff Comments.

There are no written comments that were received from the SEC staff 180 days or more before the end of our fiscal year relating to our periodic or current reports under the Securities Exchange Act of 1934.

Item 2. Properties.

HickoryTech s business is primarily focused on the provision of service and its properties are used for administrative support and to store and safeguard equipment