5179 TI40


EARLY, LENNON, PETERS & CROCKER, P.C.

ATTORNEYS AT LAW

900 COMERICA BUILDING
KALAMAZOO, MICHIGAN 49007-4752
TELEPHONE (616) 381-8844
FAX (616) 349-8525

GEORGE H. LENNON
JOHN T. PETERS, JR.
DAVID G. CROCKER
HAROLD E. FISCHER, JR.
LAWRENCE M. BRENTON
GORDON C. MILLER

BLAKE D. CROCKER
ROBERT M. TAYLOR
PATRICK D. CROCKER
ANDREW J. VORBRICH*
NICOLETTE G. HAHN**
ROBERT G. LENNON***

OF COUNSEL
VINCENT T. EARLY
HON. C. H. MULLEN
THOMPSON BENNETT

JOSEPH J. BURGIE
(1926-1992)

* Also admitted in Iowa.
** Also admitted in California and North Carolina.
*** Also admitted in New York, Illinois and Washington, D.C.


December 5, 1997



Ms. Blanca Bayo, Director
Florida Public Service Commission
2540 Shumard Oak Blvd.
Tallahassee, FL 32399-0864

971606-TX

Re: Transfer of Control of LDM Systems Inc. to RSL COM U.S.A., Inc.

Dear Ms. Bayo:

LDM Systems Inc. ("LDM"), by its attorneys, hereby advises you of the proposed transfer of control of LDM from its current shareholders to RSL COM U.S.A., Inc. ("RSL") through the sale of all of LDM's stock and request that any necessary approval of this transaction by the Florida Public Service Commission be expeditiously granted.

LDM is currently certified to provide intrastate toll telecommunications services in Florida.[1] Because LDM will continue to provide such services in Florida as a wholly-owned subsidiary of RSL, the parties will not transfer LDM's operating authority in connection with this transaction. The parties respectfully request expedited treatment of this petition in order to permit them to consummate the transaction without undue delay.

LDM is currently operating as a reseller of intrastate interexchange telecommunications service in 45 states. It also is authorized by the Federal Communications Commission to resell interstate and international service. Its address is:

---

[1] LDM was authorized by the Commission to provide intrastate telecommunications services as a reseller in Order No. PSC-92-1235-FOF-TI, in Docket No. 920841-TI, effective November 21, 1992. Moreover, LDM recently received authority to resell local service in Docket No. 97025-TX.

254 S. Main Street
New City, NY 10956
(914) 638-0001

RSL, (formerly International Telecommunications Corporation) a Delaware corporation, is a non-dominant telecommunications company engaged in the provision of domestic intrastate, interexchange, interstate and international telecommunications. By itself, and through its wholly owned subsidiaries, RSL has authority to provide intrastate, interexchange service in over 30 states. The principal office of RSL is located at:

5550 Topanga Canyon Blvd.
Suite 250
Woodland Hills, CA 91367
(818) 888-7600

On December 3, 1997, RSL and the shareholders of LDM entered into a Stock Purchase Agreement whereby RSL will acquire 100 percent of the issued and outstanding capital stock of LDM on a fully diluted basis from LDM shareholders.

After the transfer of control, LDM will continue to operate as it has in the past, using the same name, tariff and operating authority. RSL intends to retain all key LDM personnel, including certain senior management personnel. Thus, the transfer of control will be transparent to, and will have no adverse impact upon, LDM's customers.

RSL is financially qualified to acquire control of LDM and its business. A copy of RSL's most recent financial statements is attached hereto and incorporated by reference as **Attachment A.**

The transfer of control of LDM from its current shareholders to RSL is in the public interest. The addition of LDM to RSL's other telecommunication interests will enhance both RSL and LDM's ability to compete in the market for telecommunications services in Florida and elsewhere. The benefit from increased economies of scale will permit LDM to operate more efficiently and thus to compete more effectively.

In addition, as a wholly-owned subsidiary of RSL, LDM will had access to the financial resources it needs to introduce new products and services and to respond to competition in the competitive telecommunications environment in Florida. Over time, consumers in Florida will benefit from a greater number of products and service options, as well as lower prices.

Questions about this matter relating to RSL should be directed to Eric Fishman at the address indicated below:

Eric Fishman
FLETCHER, HEALD & HILDRETH, P.L.C.
11th Floor, 1300 North 17th Street
Rosslyn, VA 22209-3801
(703) 812-0400
(703) 812-0486 (facsimile)

Questions relating to LDM should be directed to the undersigned.

Wherefore, LDM respectfully requests that the Commission authorize, as promptly as possible, the transfer of control of LDM from its current shareholders to RSL so that the transaction may proceed without undue delay.

Respectfully submitted,

**LDM SYSTEMS INC.**

By: for PDC

Patrick D. Crocker
EARLY, LENNON, PETERS & CROCKER, P.C.
Attorneys for LDM

# Attachment A

## RSL's Financial Statements

# FINANCIAL QUALIFICATIONS

The parent corporation of RSL COM U.S.A., Inc. is RSL Communications, Ltd ("RSL"). Attached hereto are copies of RSL's audited financial statements for years ended December 1995 and 1996, substantiating its financial qualifications. These financial statements present current assets that exceed current liabilities by a ratio greater than 2:1. The Company's shareholders equity is also positive.

Also attached hereto is a certification by Mark J. Hirschhorn, Assistant Secretary and Global Controller of RSL. By this certification, RSL certifies that it will fully and unconditionally provide RSL COM U.S.A., Inc. with the necessary resources to continue to support RSL COM U.S.A., Inc.'s financial requirements and any other business opportunities that may arise, and that it will provide RSL COM U.S.A., Inc. with all the necessary funding to enable RSL COM U.S.A., Inc. to pay their debts when they fall due and finance their operations.

RSL is a rapidly growing multinational telecommunications company which provides a broad array of international and domestic telephone services, including long distance calling, to over 200 countries. The company currently has operations in the United States (through RSL COM U.S.A., Cyberlink, Inc. and RSL COM Primecall, Inc.), the United Kingdom, France, Germany, Sweden, Finland, Australia and Japan.

Since the release of the attached independent auditors reports, RSL has successfully raised $300 million in debt financing, and has set aside approximately $200 million of this amount primarily for acquiring, building and enhancing operations in the United States and abroad. Approximately $100 million of the remaining amount raised by RSL has been set aside in treasury securities for payment of debt instruments. Further, RSL has successfully conducted an initial public offering.

RSLCOM
RSL Communications Ltd.

# CERTIFICATION

I, Mark Hirschhorn, Assistant Secretary and Global Controller of RSL Communications, Ltd. certify that RSL Communications, Ltd., the parent company of RSL COM U.S.A., Inc. and RSL COM Primecall, Inc. (the "RSL Subsidiaries") will fully and unconditionally provide the RSL Subsidiaries with the necessary resources to continue to support the RSL Subsidiaries' financial requirements and any other business opportunities that may arise. Accordingly, RSL Communications, Ltd. will provide the RSL Subsidiaries with all necessary funding to enable the RSL Subsidiaries to pay their debts when they fall due and finance their operations.

TERESE M. FANTASIA
Notary Public, State of New York
No. 31-5009964
Qualified in New York County
Certificate Filed in New York County
Commission Expires 3/20/99

*State of New York* )
*ss)*
*County of Kings* )

*On the 10th day of June, in the year 1997 before me personally came Mark Hirschhorn to me known, who, being by me duly sworn, did depose and say that he resides in White Plains, New York that he is the Global Controller, Assistant Secretary of RSL Communications, Ltd., the Corporation described in and which executed the above instrument; and that he signed his name thereto by order of the board of directors of said corporation.*

Mark J. Hirschhorn
Assistant Secretary and Global Controller

Deloitte &
Touche LLP

Two World Financial Center
New York, New York 10281-1414

Telephone: (212) 436-2000
Facsimile: (212) 436-5000

## INDEPENDENT AUDITORS' REPORT

To the Shareholders of
RSL Communications, Ltd.

We have audited the accompanying consolidated balance sheets of RSL Communications, Ltd., a Bermuda corporation, and its subsidiaries (together, the "Company"), as of December 31, 1996 and 1995, and the related consolidated statements of operations, shareholders' equity and cash flows for the years then ended. These 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 generally accepted auditing standards in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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 audits provide a reasonable basis for our opinion.

As discussed in Note 18, the accompanying 1996 consolidated financial statements have been restated.

In our opinion, such consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Company and its subsidiaries at December 31, 1996 and 1995, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

March 7, 1997
(April 23, 1997 as to Note 18)

# RSL COMMUNICATIONS, LTD.

## CONSOLIDATED BALANCE SHEETS
## DECEMBER 31, 1996 AND 1995

| ASSETS | 1996 | 1995 |
|---|---|---|
| **CURRENT ASSETS:** | | |
| Cash and cash equivalents | $104,067,604 | $ 5,163,087 |
| Accounts receivable | 26,479,190 | 6,140,222 |
| Marketable securities - available for sale | 67,828,360 | - |
| Prepaid expenses and other current assets | 3,968,928 | 855,589 |
| Total current assets | 202,344,082 | 12,158,898 |
| MARKETABLE SECURITIES - Held to maturity | 104,370,011 | - |
| **PROPERTY AND EQUIPMENT:** | | |
| Telecommunications equipment | 29,924,892 | 9,844,196 |
| Furniture, fixtures and other | 5,926,462 | 988,898 |
| | 35,851,354 | 10,833,094 |
| Less accumulated depreciation | (3,513,449) | (302,022) |
| Property and equipment - net | 32,337,905 | 10,531,072 |
| GOODWILL AND OTHER INTANGIBLE ASSETS - Net of accumulated amortization | 87,605,112 | 29,397,768 |
| DEPOSITS AND OTHER ASSETS | 1,311,923 | 984,441 |
| TOTAL ASSETS | $427,969,033 | $ 53,072,179 |

| LIABILITIES AND SHAREHOLDERS' EQUITY | 1996 | 1995 |
|---|---|---|
| **CURRENT LIABILITIES:** | | |
| Accounts payable | $ 49,369,564 | $ 20,788,142 |
| Accrued expenses | 12,701,543 | 2,276,649 |
| Notes payable | 6,537,853 | 5,235,967 |
| Deferred revenue | 3,569,853 | 744,985 |
| Other liabilities | 5,235,961 | 2,712,054 |
| Total current liabilities | 77,414,774 | 31,757,797 |
| OTHER LIABILITIES - Noncurrent | 15,286,340 | 8,961,909 |
| LONG-TERM DEBT - Less current portion | 6,032,123 | 1,604,123 |
| SENIOR NOTES, 12¼%, due 2006, net of unamortized discount of $4,000,000 | 296,000,000 | - |
| CAPITAL LEASE OBLIGATIONS - Less current portion | 12,392,699 | 5,043,498 |
| TOTAL LIABILITIES | 407,125,936 | 47,367,327 |
| COMMITMENTS AND CONTINGENCIES | | |
| **SHAREHOLDERS' EQUITY:** | | |
| Common stock, Class A, par value $.01; no shares authorized, none issued | - | - |
| Common stock, Class B, par value $.01; 4,807,711 and 2,927,564 issued and outstanding at December 31, 1996 and 1995, respectively | 48,077 | 29,275 |
| Common stock, Class C, par value $.01; no shares issued | - | - |
| Preferred stock, par value $.01; 20,000,000 shares authorized, 9,243,866 shares issued and outstanding at December 31, 1996 and 1995, respectively | 92,439 | 92,439 |
| Warrants, common stock, exercise price of $.01 | 5,543,500 | - |
| Additional paid-in capital | 65,064,284 | 15,083,086 |
| Accumulated deficit | (47,739,777) | (9,499,948) |
| Foreign current translation adjustment | (621,926) | - |
| Deferred financing costs | (1,543,500) | - |
| Total shareholders' equity | 20,843,097 | 5,704,852 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | $427,969,033 | $ 53,072,179 |

See notes to consolidated financial statements.

# RSL COMMUNICATIONS, LTD.

## CONSOLIDATED STATEMENTS OF OPERATIONS
## YEARS ENDED DECEMBER 31, 1996 AND 1995

| | 1996 | 1995 |
|---|---|---|
| REVENUES | $113,257,340 | $ 18,616,684 |
| COST OF SERVICES | 98,461,406 | 17,510,041 |
| Gross profit | 14,795,934 | 1,106,643 |
| SELLI IG, GENERAL AND ADMINISTRATIVE EXPENSES | 38,892,751 | 9,638,997 |
| DEPRECIATION AND AMORTIZATION | 6,655,192 | 848,658 |
| Loss from operations | (30,752,009) | (9,381,012) |
| INTEREST INCOME | 3,975,922 | 172,922 |
| INTEREST EXPENSE | (11,358,796) | (193,838) |
| OTHER EXPENSE | (287,986) | - |
| FOREIGN CURRENCY TRANSACTION GAIN | 757,696 | - |
| MINORITY INTEREST | (180,100) | - |
| INCOME TAXES | (394,556) | - |
| NET LOSS | $ (38,239,829) | $ (9,401,928) |
| LOSS PER SHARE OF CLASS B COMMON STOCK | $ (11.24) | $ (3.65) |
| WEIGHTED AVERAGE NUMBER OF SHARES OF CLASS B COMMON STOCK OUTSTANDING | 3,401,464 | 2,575,855 |

See notes to consolidated financial statements.

## RSL COMMUNICATIONS, LTD.

### CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
### YEARS ENDED DECEMBER 31, 1996 AND 1995

| | Shares Common Stock Class B | Amount Common Stock Class B | Shares Preferred Stock | Amount Preferred Stock | Shares Common Stock Warrants | Amount Common Stock Warrants | Deferred Financing Costs | Additional Paid-In Capital | Accumulated Deficit | Foreign Currency Translation Adjustment | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| BALANCE, JANUARY 1, 1995 | - | $ - | - | $ - | - | $ - | $ - | $ - | $ (98,020) * | $ - | $ (98,020) |
| Issuance of preferred stock | - | - | 9,243,866 | 92,439 | - | - | - | 13,261,087 | - | - | 13,353,526 |
| Issuance of common stock | 2,927,564 | 29,275 | - | - | - | - | - | 1,821,999 | - | - | 1,851,274 |
| Net loss | - | - | - | - | - | - | - | - | (9,401,928) | - | (9,401,928) |
| BALANCE, DECEMBER 31, 1995 | 2,927,564 | 29,275 | 9,243,866 | 92,439 | - | - | - | 15,083,086 | (9,499,948) | - | 5,704,852 |
| Issuance of warrants in connection with Notes Offering | - | - | - | - | 300,000 | 4,000,000 | - | - | - | - | 4,000,000 |
| Issuance of warrants in connection with shareholder standby facility and revolving credit facility | - | - | - | - | 210,000 | 1,543,500 | (1,543,500) | - | - | - | - |
| Issuance of common stock | 1,880,147 | 18,802 | - | - | - | - | - | 49,981,198 | - | - | 50,000,000 |
| Foreign currency translation adjustment | - | - | - | - | - | - | - | - | - | (621,926) | (621,926) |
| Net loss | - | - | - | - | - | - | - | - | (38,239,829) | - | (38,239,829) |
| BALANCE, DECEMBER 31, 1996 | 4,807,711 | $ 48,077 | 9,243,866 | $ 92,439 | 510,000 | $ 5,543,500 | $ (1,543,500) | $ 65,064,284 | $ (47,739,777) | $ (621,926) | $ 20,843,097 |

*Deficit at January 1, 1995 consists of pre-operating expenses.

See notes to consolidated financial statements.

## RSL COMMUNICATIONS, LTD.

### CONSOLIDATED STATEMENTS OF CASH FLOWS
### YEARS ENDED DECEMBER 31, 1996 AND 1995

| | 1996 | 1995 |
|---|---|---|
| **CASH FLOWS (USED IN) PROVIDED BY OPERATING ACTIVITIES:** | | |
| Net loss | $ (32,239,829) | $ (9,401,928) |
| Adjustments to reconcile net loss to net cash (used in) provided by operating activities, net of effects of purchase of subsidiaries: | | |
| Accretion of interest receivable on restricted marketable securities | (1,562,359) | - |
| Depreciation and amortization | 6,655,192 | 848,658 |
| Foreign currency transaction gain | (787,696) | - |
| Loss on disposal of fixed assets | 367,658 | - |
| Provision for losses on accounts receivable | 2,829,578 | 148,690 |
| Changes in assets and liabilities: | | |
| Increase in accounts receivable | (17,033,664) | (2,453,396) |
| (Increase) decrease in deposits and other current assets | (3,249,197) | 366,210 |
| (Increase) decrease in prepaid expenses and other current assets | (925,424) | 296,867 |
| Increase in accounts payable and accrued expenses | 44,243,136 | 3,510,899 |
| Increase in deferred revenue and other current liabilities | 4,279,292 | 1,501,400 |
| (Decrease) increase in other liabilities | (7,051,860) | 8,736,770 |
| Net cash (used in) provided by operating activities | (10,475,173) | 3,554,170 |
| **CASH FLOWS USED IN INVESTING ACTIVITIES:** | | |
| Acquisition of subsidiaries | (38,552,408) | (15,413,080) |
| Purchase of marketable securities | (82,529,263) | - |
| Proceeds from marketable securities | 14,700,903 | - |
| Purchase of restricted marketable securities | (102,807,652) | - |
| Purchase of property and equipment | (15,983,227) | (1,123,539) |
| Proceeds from sale of equipment | 171,367 | - |
| Net cash used in investing activities | (225,000,280) | (16,536,619) |
| **CASH FLOWS PROVIDED BY FINANCING ACTIVITIES:** | | |
| Proceeds from issuance of common and preferred stock and warrants | 50,000,000 | 15,204,800 |
| Proceeds from notes payable | - | 3,000,000 |
| Payment of notes payable | (3,000,000) | - |
| Proceeds from issuance of 12¼% Senior Notes and warrants | 300,000,000 | - |
| Payments of offering costs | (10,988,423) | - |
| Proceeds from long-term debt - net | 44,000,000 | - |
| Payments of long-term debt | (44,598,280) | - |
| Principal payments under capital lease obligations | (382,181) | (61,799) |
| Net cash provided by financing activities | 335,031,116 | 18,143,001 |
| **INCREASE IN CASH AND CASH EQUIVALENTS** | 99,555,663 | 5,160,552 |
| **EFFECTS OF FOREIGN CURRENCY EXCHANGE RATES ON CASH** | (651,146) | - |
| **CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR** | 5,163,087 | 2,535 |
| **CASH AND CASH EQUIVALENTS, END OF YEAR** | $ 104,067,604 | $ 5,163,087 |
| **SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:** | | |
| Cash paid for: | | |
| Interest | $ 1,639,351 | $ 30,606 |
| **SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING AND FINANCING ACTIVITIES:** | | |
| Assets acquired under capital lease obligations | $ 7,897,041 | $ 4,950,333 |
| Issuance of notes to acquire stock | $ 9,328,166 | $ - |
| Issuance of warrants for shareholder standby facility | $ 1,543,500 | $ - |

See notes to consolidated financial statements.

## RSL COMMUNICATIONS, LTD.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
## YEARS ENDED DECEMBER 31, 1996 AND 1995

### 1. BUSINESS DESCRIPTION

RSL Communications, Ltd. ("RSL"), a Bermuda corporation, is the successor in interest to RSL Communications Inc., a British Virgin Islands corporation, which is the successor in interest to RSL Communications, Inc., a Delaware corporation. RSL, together with its direct and indirect subsidiaries are referred to herein as the "Company." The Company is a multinational telecommunications company which provides an array of international and domestic telephone services. The Company focuses on providing international long distance voice services to small and medium-sized businesses in strategic markets. The Company currently has operations and provides services in the United States, the United Kingdom, France, Germany, the Netherlands, Sweden and Finland. In 1995, approximately 52% of the world's international long distance telecommunications minutes originated in these markets.

### 2. ACQUISITIONS

On March 10, 1995, the Company entered into a stock purchase agreement (the "Agreement") with International Telecommunications Group, Ltd. ("ITG") and RSL COM U.S.A., Inc. (formerly known as International Telecommunications Corporation) ("RSL USA"), pursuant to which the Company initially purchased from ITG 66,667 shares of ITG's Series A convertible preferred stock (which represented 25% of ITG's then outstanding stock, including common and preferred shares) for $3,000,000, subject to increase, to a maximum of $4,750,000. Such increase was predicated upon the attainment of certain financial targets and ratios. Based on the terms of the Agreement, the adjusted purchase price of the shares totaled $4,750,000. The Company subsequently purchased additional shares of ITG's common stock at various times during 1996 and 1995 for a total purchase price of cash and secured notes aggregating $26,725,000 and $12,870,000 at December 31, 1996 and 1995, respectively, and the assumption of net liabilities resulting in recorded goodwill of $26,780,000. At December 31, 1996, the Company's investment in ITG was $54,204,000, which represented in excess of 87% of the outstanding shares of ITG.

Effective September 1, 1995, ITG's subsidiary, RSL USA, purchased 51% of the capital stock of Cyberlink, Inc. ("Cyberlink"). During the period August 1996 through December 1996, RSL USA purchased 1,023,807 shares of the capital stock of Cyberlink for approximately $7,200,000. In addition, through March 1997, the Company acquired the remaining outstanding shares.

The total purchase price consisted of approximately $11,509,000, and assumption of net liabilities of $21,131,000. In connection with the purchase of Cyberlink, the Company recorded approximately $32,640,000 of goodwill.

In November 1995, the Company, through its wholly-owned subsidiary, RSL COM Europe, Ltd. ("RSL COM Europe"), completed the acquisition of 51% of Cyberlink Communications Europe Ltd. ("Cyberlink Europe"). Cyberlink Europe is a holding company which owned 100% of the shares of RSL COM Sweden AB, Cyberlink International Telesystems Germany GmbH and RSL COM Finland OY. During the period August 1996 through March 1997, RSL COM Europe purchased the remaining 49% of the Cyberlink Europe shares for approximately $2,062,000. The total cash paid was approximately $3,805,000 at December 31, 1996. The Company recorded approximately $2,457,000 of goodwill in connection with this purchase.

In May 1996, the Company acquired the net assets, principally telecommunications equipment and facilities, constituting the international long distance voice businesses of Sprint in France and Germany through its wholly-owned subsidiaries, RSL COM France S.A., a French corporation ("RSL France"), and RSL COM Deutschland GmbH, a German limited liability company ("RSL Germany").

Pursuant to the applicable asset purchase agreements, the Company can not disclose the purchase price of the net assets. In connection with this transaction, the Company recorded approximately $7,905,000 of goodwill.

In October 1996, the Company acquired 38,710 shares of Belnet Nederland B.V. ("Belnet/RSL"), representing 75% of the outstanding stock for $10,000,000. In connection with the purchase of Belnet/RSL, the Company recorded approximately $8,000,000 of goodwill.

In August 1996, the Company acquired the assets and assumed certain limited liabilities of Incom (UK) Limited ("Incom"), a United Kingdom reseller, for $500,000 plus 3,954 nonvoting shares of ITG (the "Purchased Shares"). In addition, 3,333 voting shares of ITG currently held by Incom were exchanged for an equal number of nonvoting shares. The Company has also entered into a consulting agreement with an affiliate of Incom calling for payments of $10,000 per month for seven years and has paid such affiliate $280,000 for its agreement not to compete for a period of seven years and has agreed to make a $660,000, seven-year loan to such affiliate, bearing interest at a rate of 7% per annum. In connection with this acquisition, the Company recorded approximately $3,840,000 of goodwill. The Company will fully evaluate the acquired assets prior to August 1997. The Company does not expect any material changes to its recorded asset values as a result of such evaluation.

The acquisitions have been accounted for by the purchase method of accounting and, accordingly, the purchase prices have been allocated to the assets acquired, primarily fixed assets and accounts receivable, and liabilities assumed based on their estimated fair values at the dates of acquisition. The excess of the purchase price over the estimated fair values of the net assets acquired has been recorded as goodwill, which is amortized over fifteen years.

The December 31, 1995 consolidated statements of operations, shareholders' equity and cash flows include the results of ITG, Cyberlink and Cyberlink Europe from their dates of acquisition, respectively, through December 31, 1995. The December 31, 1996 consolidated statements of operations, shareholders' equity and cash flows also include the results of RSL COM France and RSL COM Germany as of May 1996 (date of commencement of operations), Incom as of August 1996, and Belnet/RSL from October 1996 (date of acquisition) through December 31, 1996.

The following presents the unaudited pro forma consolidated statement of operations of the Company for the years ended December 31, 1996 and 1995 as though the acquisitions of ITG, Cyberlink, Cyberlink Europe, RSL COM France, RSL COM Germany and Belnet/RSL had occurred on January 1, 1995. The acquisition of Incom is excluded as it is not significant. The consolidated statement does not necessarily represent what the Company's results of operations would have been had such acquisitions actually occurred on such date.

| | Year Ended December 31, 1996 (Unaudited) | Year Ended December 31, 1995 (Unaudited) |
|---|---|---|
| Revenues | $124,235,934 | $ 72,777,643 |
| Net loss | $ (41,277,456) | $ (38,008,282) |
| Net loss per share | $ (12.14) | $ (14.76) |

## 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

*Principles of Consolidation and Basis of Presentation* - The consolidated financial statements include the accounts of RSL Communications, Ltd. and its majority-owned subsidiaries: its 87% owned subsidiary, ITG, and its 94% owned subsidiary, Cyberlink, Inc., and RSL COM Europe and its 91% owned subsidiary, Cyberlink Communications Europe Ltd., and Belnet/RSL, a 75% owned subsidiary of RSL COM Europe. The Company has included 100% of its subsidiaries' operating losses since the minority interests' investments have been reduced to zero. Minority interest represents another entity's ownership interest in Belnet/RSL at December 31, 1996. All material intercompany accounts and transactions have been eliminated. All of the Company's subsidiaries' years end December 31.

*Management Assumptions* - The preparation of the consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. Such estimates primarily relate to reserves recorded for doubtful accounts and accruals for other claims. Actual results could differ from these estimates.

*Foreign Currency Translation* - Assets and liabilities of foreign entities have been translated into United States dollars using the exchange rates in effect at the balance sheet dates. Results of operations of foreign entities are translated using the average exchange rates prevailing throughout the period. Local currencies are considered the functional currencies of the Company's foreign operating entities. The Company utilizes a net settlement process with its correspondents comprised of special drawing rights ("SDRs"). SDRs are the established method of settlements among international telecommunications carriers. The SDRs are valued based upon the values of a basket of foreign currencies. Translation effects are accumulated as part of the cumulative foreign currency translation adjustment in equity which at December 31, 1995 were not significant. Gains and losses from foreign currency transactions are included in the consolidated statements of operations for each respective period.

*Cash and Cash Equivalents* - The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents.

*Accounts Receivable* - Accounts receivable are stated net of the allowance for doubtful accounts of $3,900,000 and $1,600,000 at December 31, 1996 and 1995, respectively. The Company recorded bad debt expense of $2,829,578 and $148,690 for the years ended December 31, 1996 and 1995, respectively.

*Accrued Expenses* - Accrued expenses for the years ended December 31, 1996 and 1995 consist primarily of accrued interest. Accrued interest for the years ended December 31, 1996 and 1995 were $9,447,000 and $92,000, respectively.

*Marketable Securities* - Marketable securities consist principally of U.S. Treasury bills, commercial paper and corporate notes with a maturity date greater than three months when purchased. Available for sale securities are stated at market and the held to maturity securities are stated at amortized costs. Gains and losses, both realized and unrealized, are measured using the specific identification method. Market value is determined by the most recently traded price of the security at the balance sheet date. Marketable securities are defined as either available for sale or held to maturity securities under the provisions of SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," depending on the security.

*Property and Equipment and Related Depreciation* - Property and equipment are stated at cost or fair values at the date of acquisition, and in the case of equipment under capital leases, the present value of the future minimum lease payments, less accumulated depreciation. Deprecation is calculated using the straight-line method over the estimated useful lives of the depreciable assets, which range from five to fifteen years. Improvements are capitalized, while repair and maintenance costs are charged to operations as incurred.

*Goodwill* - Goodwill represents the excess of cost over the fair value of the net assets of acquired entities, and is being amortized using the straight-line method over fifteen years. The Company periodically reviews the value of its goodwill to determine if an impairment has occurred. The Company measures the potential impairment of recorded goodwill by the undiscounted value of expected future cash flows in relation to its net capital investment in the subsidiary. Based on its review, the Company does not believe that an impairment of its goodwill has occurred.

*Deferred Financing Costs* - The deferred financing costs incurred in connection with the Senior Notes are being amortized on a straight-line basis over ten years.

*Deposits* - Deposits consist principally of amounts paid to the Company's carrier vendors.

*Revenue Recognition and Deferred Revenue* - The Company records revenue based on minutes (or fractions thereof) of customer usage.

The Company records payments received in advance for prepaid calling card services and services to be supplied under contractual agreements as deferred revenues until such related services are provided.

*Costs of Services* - Costs of services is comprised primarily of transmission costs.

*Selling Expenses* - Selling costs such as commissions, marketing costs, and other customer acquisition costs are treated as period costs. Such costs are recorded in selling, general and administrative costs in the Company's statement of operations.

*Income Taxes* - The Company accounts for income taxes under the provisions of Statement of Financial Accounting Standards ("SFAS") No. 109, Accounting for Income Taxes. SFAS No. 109 establishes financial accounting and reporting standards for the effect of income taxes that result from activities during the current and preceding years. SFAS No. 109 requires an asset and liability approach for financial reporting for income taxes. The Company's foreign subsidiaries file separate income tax returns in the jurisdiction of their operations. The Company's United States subsidiaries file stand-alone United States income tax returns.

*Loss Per Common Share* - Loss per common share is calculated by dividing the loss attributable to common shares by the weighted average number of shares outstanding. Outstanding common stock options and warrants are not included in the loss per common share calculation as their effect is anti-dilutive.

*New Accounting Standards* - During 1995, the Company adopted SFAS No. 121, Impairment of Long-Lived Assets. There was no adjustment recorded as a result of adopting this standard. The Company periodically compares the carrying value of its long-lived assets, principally property and equipment, to undiscounted cash flows generated by the long-lived assets. The Company's undiscounted cash flows exceed the carrying value of its long-lived assets.

## 4. CONCENTRATION OF CREDIT RISK

The Company is subject to significant concentrations of credit risk which consist principally of trade accounts receivable, cash and cash equivalents, and marketable securities. The Company's U.S. subsidiaries sell a significant portion of their services to other carriers and, as a result, maintain significant receivable balances with certain carriers. If the financial condition and operations of these customers deteriorate below critical levels, the Company's operating results could be adversely affected.

The Company now performs ongoing credit evaluations of its customers' financial condition and requires collateral in the form of deposits in certain circumstances.

The Company maintains its cash with high quality credit institutions, and its cash equivalents and marketable securities are in high quality securities.

## 5. MARKETABLE SECURITIES

A summary of the Company's available for sale marketable securities at December 31, 1996 is as follows:

| | Amortized Cost | Market Value |
|---|---|---|
| Corporate notes | $40,728,408 | $40,677,564 |
| Medium term notes | 10,950,557 | 10,938,389 |
| Commercial paper | 10,260,965 | 10,256,634 |
| Federal agency notes | 5,888,430 | 5,884,481 |
| | $67,828,360 | $67,757,068 |

The Company has recorded its available for sale marketable securities at amortized cost as the difference between amortized cost and market value is immaterial to the consolidated financial statements.

The carrying value of the available for sale marketable securities by maturity date as of December 31, 1996 is as follows:

| | |
|---|---|
| Matures in one year | $57,548,581 |
| Matures after one year through three years | 10,279,779 |
| Total | $67,828,360 |

Proceeds from the sale of available for sale marketable securities during 1996 were $14,700,903. Gross gains of $56,302 were realized on these sales in 1996.

Securities classified as held to maturity, which are comprised of Federal agency notes, are stated at amortized cost. Such securities are restricted in order to make the first six scheduled interest payments on the 12-1/4% Senior Notes. The held to maturity securities at December 31, 1996 are as follows:

| | Amortized Cost | Market Value |
|---|---|---|
| Matures in one year | $ 39,692,258 | $ 39,738,512 |
| Matures after one year through three years | 64,677,753 | 65,001,563 |
| Total | $ 104,370,011 | $ 104,740,075 |

## 6. INCOME TAXES

The Company has incurred losses since inception for both book and tax purposes. The Company's Netherlands subsidiary recorded approximately $395,000 in income tax expense. For the years ended December 31, 1996 and 1995, the Company had net operating loss carryforwards generated primarily in the United States of approximately $47,000,000. The net operating loss carryforwards will expire at various dates beginning in 2009 through 2012 if not utilized.

In accordance with SFAS No. 109, the Company has computed the components of deferred income taxes as of December 31, 1996 and 1995, as follows:

| | 1996 | 1995 |
|---|---|---|
| Deferred tax assets | $ 18,800,000 | $ 6,900,000 |
| Less valuation allowance | (18,800,000) | (6,900,000) |
| Net deferred tax assets | $ - | $ - |

The Company's net operating losses and legal reserves generated the deferred tax assets. At December 31, 1996 and 1995, a valuation allowance of $18,800,000 and $6,900,000, respectively, is provided as the realization of the deferred tax benefits is not likely.

## 7. NOTES PAYABLE AND LONG-TERM DEBT

On October 3, 1996, RSL Communications PLC ("RSL PLC"), a wholly-owned subsidiary of RSL, issued (the "Private Offering") 300,000 Units, each consisting of an aggregate of one $1,000 Senior Note (collectively, the "Notes") due 2006 bearing interest at the rate of 12-1/4% and one warrant to purchase 1.815 Class A common shares which expire in ten years (collectively, the "Warrants"). The exercise price of such Warrants is $.01.

The value ascribed to the Warrants was $4,000,000. The unamortized discount of $4,000,000 is recorded as a reduction against the face value of the Notes, and is amortized over the life of the Notes.

The Notes, which are guaranteed by RSL, are redeemable, at RSL PLC's option, subsequent to November 15, 2001, initially at 106.1250% of their principal amount, declining to 103.0625% of their principal amount for the calendar year subsequent to November 15, 2002, and at 100% of the principal amount subsequent to November 15, 2003.

The indenture pursuant to which the Notes were issued contains certain restrictive covenants which impose limitations on RSL and certain of its subsidiaries' ability to, among other things: (i) incur additional indebtedness, (ii) pay dividends or make certain other distributions, (iii) issue capital stock of certain subsidiaries, (iv) guarantee debt, (v) enter into transactions with shareholders and affiliates, (vi) create liens, (vii) enter into sale-leaseback transactions, and (viii) sell assets.

At December 31, 1996, the Company is in compliance with the above restrictive covenants.

The Company is obligated to register the Notes with the Securities and Exchange Commission on or prior to June 1, 1997. If the Notes are not registered on or prior to June 1, 1997, the interest rate on the Notes will increase to 12-3/4%.

In connection with the issuance of the Notes, the Company is required to maintain restricted marketable securities in order to make the first six scheduled interest payments on the Notes. Such restricted marketable securities amounted to $104,370,011 at December 31, 1996.

At December 31, 1996, the Company had a $35,000,000 shareholder standby facility with the Company's Chairman and a $15,000,000 revolving credit facility with a bank (the "Revolving Credit Facility"), guaranteed by the Company's Chairman, all of which was available.

The shareholder standby facility bears interest at the rate of 11% per annum. In connection with this facility and the Company's Chairman's personal guarantee of the Revolving Credit Facility, the Company's Chairman received warrants, which vest over one year, to purchase 210,000 Class B common shares of the Company (the "Class B Common Stock"). The Company recorded $1,543,500 as the value of the warrants at the time of their issuance. At December 31, 1996, the deferred financing costs recorded will be amortized, over the vesting period, through October 3, 1997. The revolving credit facility bears interest at the rate of LIBOR plus 1%.

The warrants become exercisable on October 3, 1997 at an exercise price of $.01 per share and expire in October 2006.

In connection with the September 1996 purchase of additional shares of ITG's common stock, the Company issued secured notes totaling approximately $9,328,000. Such notes and interest are secured by the common stock acquired, and are payable in quarterly annual installments, and bear interest at the rate of 6%.

During August 1996, the Company obtained a $50,000,000 revolving credit facility with a bank, guaranteed by the Company's Chairman, and utilized this facility to repay the bank for all amounts due under the previously outstanding revolving loan facility provided by the bank and guaranteed by the Company's Chairman, which was $44,000,000 at the time of repayment. Immediately prior to the Private Offering, the Company repaid $35,000,000 of the $44,000,000 borrowed under the Revolving Credit Facility with the proceeds of the Subordinated Shareholder Loan (see Note 11) and reduced the outstanding commitment under the Revolving Credit Facility to $15,000,000.

At December 31, 1996, RSL USA has a series of current notes payable to different vendors in the amount of $213,086, which bear interest at the rates from 8% to 14.5%. At December 31, 1995, such amount was $698,652, of which $564,529 was current.

Cyberlink has a credit agreement which provides for up to $5,000,000 in committed credit lines to finance its accounts receivable. Interest is payable at 2-1/4% over the prime rate of interest (prime being 8.25% at December 31, 1996). A second credit line provides for up to $2,000,000 in capital expenditure financing. Interest on this line is payable at 2-1/2% over the prime rate of interest. The total amounts outstanding at December 31, 1996 from the above credit lines were $679,784 and $605,600, respectively, and $1,566,000 and $470,000, at December 31, 1995, respectively. The credit lines terminate on August 31, 1998. Borrowings under both of these credit lines are collateralized by a security interest in substantially all of Cyberlink's assets.

Cyberlink has a long-term note payable to a vendor in the amount of $1,743,000 which bears interest at the rate of 10%, commencing January 1, 1997.

One of the Company's primary equipment vendors has provided to certain of the Company's subsidiaries an aggregate of approximately $50 million in vendor financing commitments to fund the purchase of additional capital equipment. At December 31, 1996, approximately $39.0 million was available. Borrowings under this agreement are recorded as capital lease obligations.

Long-term debt matures as follows:

| | |
|---|---|
| 1997 | $ 6,537,853 |
| 1998 | 3,099,349 |
| 1999 | 2,932,774 |
| 2000 | - |
| 2001 | - |
| 2002 and thereafter | 300,000,000 |
| Total | 312,569,976 |
| Less current maturities | (6,537,853) |
| Long term debt and 12-1/4% senior notes | $306,032,123 |

RSL's notes payable had fair values that approximated their carrying amounts.

Interest expense on the above notes was approximately $10,456,869 and $461,000 for the years ended December 31, 1996 and 1995, respectively.

## 8. GOODWILL AND OTHER INTANGIBLE ASSETS

Intangible assets at December 31, 1996 and 1995 consist of the following:

| | 1996 | 1995 |
|---|---|---|
| Goodwill | $79,731,497 | $29,425,093 |
| Deferred financing costs | 10,988,423 | - |
| Organization costs and others | 625,820 | 521,086 |
| | 91,345,740 | 29,946,179 |
| Less accumulated amortization | (3,740,628) | (548,411) |
| Intangible assets - net | $87,605,112 | $29,397,768 |

Amortization expense for the years ended December 31, 1996 and 1995 was $3,192,217 and $548,411, respectively.

## 9. SHAREHOLDERS' EQUITY

*Common Stock* - During 1996, the Company issued 1,880,147 shares of Class B Common Stock for cash aggregating $50,000,000. During 1995, 2,927,564 shares were issued for $1,851,274. The Company is authorized to issue 20,000,000 shares in aggregate of its common stock.

*Preferred Stock* - During 1995, the Company issued 9,243,866 shares of its preferred stock to the holders of its Class B common stock for cash of $13,353,526. The preferred stock ranks senior to the Company's common stock as to dividends and a liquidation preference of $1,000 per share. Each share is convertible at the holder's option into one share of Class B Common Stock. All preferred shares will be automatically converted into the Company's Class B Common Stock in the event of the consummation of a public offering that yields proceeds in excess of $25,000,000. Dividends, at the rate of 8%, are cumulative. Upon conversion of the shares of the preferred stock, the cumulative dividends are not payable and are to be deemed canceled and waived. The cumulative amount of such dividends is approximately $16,000.

## 10. CAPITAL LEASE OBLIGATIONS

Future minimum annual payments applicable to assets held under capital lease obligations for years subsequent to December 31, 1996 are as follows:

| | |
|---|---|
| 1997 | $ 1,237,477 |
| 1998 | 2,852,380 |
| 1999 | 4,355,684 |
| 2000 | 3,691,498 |
| 2001 | 2,626,885 |
| 2002 and thereafter | 3,769,417 |
| Total minimum lease obligations | 18,533,341 |
| Less interest | (5,704,476) |
| Present value of future minimum lease obligations | 12,828,865 |
| Less current portion, included in other current liabilities | (436,166) |
| Long-term lease obligations at December 31, 1996 | $ 12,392,699 |

The assets and liabilities under capital leases are recorded at the present value of the minimum lease payments using effective interest rates ranging from 9% to 11% per annum.

Assets held under capital leases aggregated $13,224,507 and $5,325,771 at December 31, 1996 and 1995, respectively. The related accumulated depreciation was $824,933 and $82,077, respectively.

## 11. RELATED PARTY TRANSACTIONS

In September 1996, the Company borrowed $35,000,000 from Ronald S. Lauder, the Chairman of the Board of the Company and the principal shareholder of the Company, bearing interest at the rate of

11% per annum (the "Subordinated Shareholder Loan"). The Company repaid the Subordinated Shareholder Loan with the proceeds of the Shareholder Equity Investment (described below).

The Company used the proceeds of the Subordinated Shareholder Loan to repay $35,000,000 of the amounts outstanding under the Revolving Credit Facility available in August 1996 (see Note 7) and reduced the outstanding commitment amount under the Revolving Credit Facility to $15,000,000. The Revolving Credit Facility is personally guaranteed by the Company's Chairman.

Prior to the closing of the Private Offering, Ronald S. Lauder, the Company's Chairman, Leonard A. Lauder, a director of the Company and Ronald S. Lauder's brother, and Lauder Gaspar Venture LLC ("LGV"), an investment vehicle the principal investors of which are Ronald S. Lauder and Leonard A. Lauder and the managing member (through a wholly-owned company) of which is Andrew Gaspar, a director of the Company, purchased an aggregate of 1,880,147 shares of Class B Common Stock (approximately 11.6% of the outstanding common shares of the Company on a fully diluted basis) for $50,000,000 (the "Shareholder Equity Investment"). LGV purchased one-half of such shares and Ronald S. Lauder and Leonard A. Lauder each purchased one-quarter of such shares.

In addition, Ronald S. Lauder will, upon the request of the Company, provide (or arrange for a bank to provide) the Company with the Shareholder Standby Facility (see Note 7). If this facility is provided by a bank, Mr. Lauder will personally guarantee the Company's obligations under the facility up to $35,000,000. Under the terms of the indenture which governs the Notes, the Company may borrow, repay, and reborrow any amounts under the Shareholder Standby Facility at any time or from time to time. However, the lender will be obligated to make loans thereunder at the request of the Company up to $35,000,000, without conditions and regardless of any default thereunder, until such time as the Company has received $35,000,000 of net cash proceeds from the issuance of common shares of the Company (the "Common Stock"). The Shareholder Standby Facility will expire on the earlier of December 15, 2006 or the receipt of $35,000,000 of net cash proceeds from the issuance of Common Stock and will provide that interest may not be paid in cash until December 15, 2001.

Nesim N. Bildirici, a director and the Vice President of Mergers and Acquisitions of the Company, is an employee of both the Company and R.S. Lauder, Gaspar & Co., L.P. ("RSLAG"), a venture capital company owned and controlled by Ronald S. Lauder and Andrew Gaspar. Mr. Bildirici's salary is paid by RSLAG and the Company reimburses RSLAG each year for the services Mr. Bildirici provides to the Company. In 1996, the Company reimbursed RSLAG approximately $130,000 for Mr. Bildirici's services. Mr. Bildirici currently dedicates substantially all of his business time to the business of the Company and is expected to continue to do so for the foreseeable future.

RSL Management Corporation ("RSL Management"), which is wholly-owned by Ronald S. Lauder, the Chairman of the Board of the Company and the principal shareholder of the Company, leases an aggregate of 2,670 square feet of office space to the Company at an annual rent of $180,000 per annum. In addition, RSL Management provides payroll and benefit services to the Company for an annual fee of $6,000.

The Company has employment contracts with certain of its executive officers. These agreements expire beginning April 1998 through May 2000 unless terminated earlier by the executive or by the Company, and provide for annual salaries and bonuses based on the performance of the Company. Salary expense for these officers was approximately $1,419,000 and $646,250 for the years ended December 31, 1996 and 1995, respectively. The aggregate commitment for annual future salaries at

December 31, 1996, excluding bonuses, is approximately $1,727,500, $1,051,000, $447,875 and $66,667 for 1997, 1998, 1999 and 2000, respectively.

## 12. DEFINED CONTRIBUTION PLAN

In 1996, the Company instituted a defined contribution plan which provides for retirement benefits for most of its domestic employees. The Company's contributions to the defined contribution which are based on a percentage of the employee's annual compensation subject to certain limitations, were not significant for 1996.

## 13. STOCK INCENTIVE PLAN

In April 1995, the Company established an Incentive Stock Option Plan (the "Plan") to reward employees, nonemployee consultants and directors for service to the Company and to provide incentives for future service and enhancement of shareholder value. The Plan is administered by the Compensation Committee of the Board of Directors of the Company (the "Committee"). The Committee consists of three members of the Board of Directors. The Plan provides for awards of up to 1,000,000 shares of Class B common stock of the Company.

The options granted in 1995 vest over a period of three years commencing on the first anniversary of the date of grant such that the option holder may not acquire more than 2% of the outstanding capital stock as of the date upon which the related employment agreement expires. The options granted in 1996 vest in one-third increments on each of the first, second and third anniversaries of the grant date.

| | Number of Options | Exercise Price | Weighted Average Exercise Price |
|---|---|---|---|
| Outstanding at January 1, 1995 | | | |
| Granted | 650,000 | $ 0.001 | $ 0.001 |
| Exercised | - | - | - |
| Rescinded/canceled | - | - | - |
| Outstanding at December 31, 1995 | 650,000 | 0.001 | 0.001 |
| Granted | 129,600 | 3.50-5.50 | 3.79 |
| Exercised | - | - | - |
| Rescinded/canceled | - | - | - |
| Outstanding at December 31, 1996 | 779,600 | $0.001-$5.50 | $ 0.63 |

| | Exercisable | Rerserved for Future Grants | Weighted Average Exercise Price |
|---|---|---|---|
| December 31, 1996 | 81,142 | 220,400 | $ 0.001 |
| December 31, 1995 | - | 350,000 | - |

The Company has elected to follow Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* ("APB 25") and related Interpretations in accounting for employee stock options. The Company has issued its options at fair market value at the date of grant. Under APB 25, because the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized.

SFAS Statement No. 123, *Accounting for Stock-Based Compensation* ("SFAS 123") was issued by the FASB in 1995 and if fully adopted, changes the methods for recognition of costs on plans similar to those of the Company. Adoption of the recognition provisions of SFAS No 123 is optional; however, pro forma disclosures as if the Company adopted the cost recognition requirements under SFAS No. 123 is presented below.

Under SFAS No. 123, options granted during 1996 and 1995, the fair value at the date of grant was estimated using the Black-Scholes option pricing model. The fair value was estimated using the minimum value method. Under this method, the expected volatility of the Company's common stock is not estimated, as there is no market for the Company's common stock in which to monitor stock price volatility.

The following weighted average assumptions were used in calculating the fair value of the options granted in 1996 and 1995, respectively: risk-free interest rates of 5.85%; no dividends are expected to be declared; expected life of the options are between 30 and 42 months and between 39 and 51 months, respectively; and a maximum contractual life of 10 years.

For purposes of the pro forma disclosures the estimated fair value of the options granted is amortized to compensate expense over the options' vesting period. The Company's pro forma information is as follows:

| | 1996 | 1995 |
|---|---|---|
| Net loss: | | |
| As reported | $(38,239,829) | $ (9,401,928) |
| Pro forma | $(38,314,829) | $ (9,404,428) |
| Net loss per common share: | | |
| As reported | $ (11.24) | $ (3.65) |
| Pro forma | $ (11.26) | $ (3.65) |
| Weighted average fair falue of options granted during the year | $ 0.58 | $ 0.0004 |

## 14. COMMITMENTS AND CONTINGENCIES

At December 31, 1996, the Company was committed to unrelated parties for the rental of office space under operating leases. Minimum annual lease payments with respect to the leases is as follows:

| Year Ended December 31, | |
|---|---|
| 1997 | $ 2,117,442 |
| 1998 | 1,851,834 |
| 1999 | 1,641,577 |
| 2000 | 1,489,268 |
| 2001 | 1,426,569 |
| 2002 and thereafter | 3,302,871 |
| | $11,829,561 |

Rent expense for the years ended December 31, 1996 and 1995 was $2,275,721 and $209,806, respectively.

The Company is committed to pay for transmission capacity under certain operating leases. The minimum annual lease payments with respect to these agreements is as follows:

| Year Ended December 31, | |
|---|---|
| 1997 | $40,500,000 |
| 1998 | 3,000,000 |
| | $43,500,000 |

The minimum lease payments for the year ended December 31, 1996 were $21,500,000. The Company did not remit payments for this full amount. At December 31, 1996 and 1995, the Company had accrued approximately $8,000,000 and $5,900,000, respectively, as purchase accounting adjustments representing the unfavorable portion of such lease commitments. Concurrent with the consummation of the purchase of the capital stock of Cyberlink, the Company obtained transmission capacity. At December 31, 1995, the Company recorded what management believed to be its best estimate of the unfavorable portion related to the operating leases. Prior to December 31, 1996, the Company recorded what management believed to be its best estimate of the unfavorable portion related to the operating leases and the liabilities incurred in connection with the early termination or reconfiguration of the existing operating leases. Such purchase accounting accruals have been recorded under the captions "Goodwill" and "Other Liabilities - Noncurrent" in the accompanying consolidated balance sheets. When the Company ultimately terminates, settles or reconfigures its operating leases, the Company will recognize the different between the approximately $8,000,000 recorded at December 31, 1996 and the actual cost incurred to terminate, settle or reconfigure the operating leases. Such amount will be recorded in the Company's consolidated statement of operations. The amount incurred when combined with the payments remitted during the year ended December 31, 1996, aggregated approximately $21,500,000. The Company is currently negotiating the amendment or termination of these leases.

*Commitments and Contingencies* - The Company is involved in various claims that arose in the ordinary course of its acquired businesses prior to the Company's acquisition of such businesses. The expected settlements from these matters have been accrued and are recorded as "Other Liabilities." In management's opinion, the settlement of such claims would not have a material adverse effect on the Company's consolidated financial position or results of its operations.

*Letters of Credit*- The Company has outstanding letters of credit aggregating $550,000 at December 31, 1996, expiring at various dates. Such letters of credit, which were issued as deposits to vendors or security on leased premises, are fully secured by certificates of deposit, and are classified as current assets.

## 15. SIGNIFICANT CUSTOMER

For the year ended December 31, 1996, no customer accounted for more than 10% of the Company's revenues. For the year ended December 31, 1995, one customer accounted for 26% of the Company's revenues.

## 16. REVENUES BY GEOGRAPHIC AREA

The following table provides certain geographic data on the Company's operations for the year ended December 31, 1996 and 1995:

| | Revenues | Operating Income (Loss) | Identifiable Assets |
|---|---|---|---|
| 1996: | | | |
| United States | $ 85,842,924 | $ (12,146,118) | $ 54,509,115 |
| Germany | 8,844,479 | (2,249,834) | 9,776,032 |
| France | 7,345,625 | (886,119) | 10,423,464 |
| United Kingdom | 6,260,032 | (7,966,674) | 18,994,422 |
| Netherlands | 3,471,165 | 1,087,142 | 8,605,557 |
| Corporate and other | 1,493,115 | (8,300,796) | 325,660,443 |
| | $113,257,340 | $ (30,462,399) | $427,969,033 |
| 1995: | | | |
| United States | $ 18,460,486 | $ (6,969,473) | $ 37,759,621 |
| Germany | - | - | - |
| France | - | - | - |
| United Kingdom | - | - | - |
| Netherlands | - | - | - |
| Corporate and other | 156,198 | (2,411,539) | 15,312,558 |
| | $ 18,616,684 | $ (9,381,012) | $ 53,072,179 |

Intersegment and intergeographic revenue are not significant to the revenue of any business segment or geographic location. There is no export revenue from the United States. Corporate and other assets consist principally of cash and cash equivalents and goodwill.

## 17. SUMMARIZED FINANCIAL INFORMATION

The following presents summarized financial information of RSL Communications PLC ("RSL PLC") as of December 31, 1996. RSL PLC was incorporated in 1996 and is a 100% wholly-owned subsidiary of the Company. RSL PLC had no independent operations other than serving solely as a foreign holding company for the Company's U.S. and European operations. The Notes issued by RSL PLC are fully and unconditionally guaranteed by the Company. The Company's financial statements are, except for the Company's capitalization, corporate overhead expenses and available credit facilities, identical to the financial statements of RSL PLC.

| | December 31, 1996 |
|---|---|
| Current assets | $201,734,395 |
| Noncurrent assets | $225,131,081 |
| Current liabilities | $ 74,949,341 |
| Noncurrent liabilities | $394,555,559 |

| | Year Ended December 31, 1996 |
|---|---|
| Net revenues | $113,257,340 |
| Gross profit | $ 14,795,934 |
| Net loss | $ (34,309,127) |

## 18. RESTATEMENT

Subsequent to the issuance of the Company's 1996 consolidated financial statements, the Company's management determined that a value should have been assigned to its warrants upon issuance, which previously had not been assigned a value. As a result, the Company's 1996 consolidated financial statements have been restated from the amounts previously reported to reflect the assignment of a value to its warrants.

The effect of the restatement on the 1996 consolidated financial statements was to increase total shareholders' equity by $4,000,000 and to reduce the senior notes by $4,000,000.

* * * * * *