2016 Annual Report

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April 7, 2017

Dear Shareholders,

This is my first letter to you since I joined our Company in October of last year. It has been a period of intense activity over the past six months as we chart a clear and ambitious path forward. I would like to share what we have done, where we are headed, and why I firmly believe that the future holds enormous opportunity for TeraGo.

A REAL OPPORTUNITY

The digital transformation of our society and economy represents significant business potential for TeraGo. New applications are changing business models in every industry. The speed of change is forcing businesses of every size to rethink how they operate, deploy resources and connect their people and customers.

As a result, we are seeing clear trends that positively impact our business. The managed third-party cloud model is seeing tremendous uptick, with mid-market companies (between 100 and 500 employees) dedicating new spend and effort in this area. Research shows that key verticals in this segment (such as financial services, business services, utilities and the public sector) will see between 24 and 33% CAGR in public and private cloud investments in the coming years.

This and other positive trends present a real business growth opportunity for TeraGo. With a broad and growing customer base, and a strong Canadian integrated telecom stack (network, cloud & data centres) – we have an offering matched only by very large telcos and cablecos.

Yet, we can move with greater speed to seize new opportunity and help our customers succeed. We can help them enable new IT solutions, deploy new applications, track customer interactions and collect and process massive volumes of data. As businesses increasingly move IT workloads to external environments to accelerate and improve their performance, we have the capability to partner with them to ensure the processes are in place and the integrity and security of their data is maintained.

SHARPENED FOCUS – CLEAR STRATEGIC DIRECTION

With this in mind, we sharpened our focus.

We will concentrate our growth efforts on the significant opportunity in the mid-sized market in Canada – organizations that require enterprise services, with carrier-grade performance, but are largely underserved by giant telecom and cable competitors. We will target this market with the right offer, delivered and supported in the right way.

In parallel, we will continue to nurture and grow our large base of small business customers – entrepreneurs, challengers, early-stage and established smaller players that make up a significant part of our current base, and the majority of the Canadian market.

Combined, this balance of growth targeting and customer service excellence will deliver results over the long term. And, TeraGo is perfectly positioned to win.

The organizations we serve and want to serve all have common characteristics: they need solutions and advice tailor-made for their scale and their specific requirements. We understand their challenges and their goals – because we share them. We live in their reality, share their aspirations and recognize their limitations. We will arm them with enterprise-class solutions that fit their needs. We will help them to level the playing field against larger incumbents and win in competitive markets. And, we will do so as a partner – focused on service, determined to add value.

BUILDING FOR GROWTH

Informed by this clear strategic direction, we've been hard at work. Over the past several months, we have taken important steps forward:

NEW LEADERSHIP: We strengthened the team and attracted world-class leaders with a strong track record of successfully driving change and growth in this market.

SERVICE PORTFOLIO RELAUNCH: We streamlined and re-launched our entire portfolio of services at the beginning of April 2017 to better align to customer needs and improve sales efficiency. We also enhanced our offers to feature in-demand services and improve the customer experience. For example:

- We simplified and reduced the number of purchasable products and features (SKUs) by over 60% - from 350 to 130 – matching customer demand across our Connectivity, Cloud and Co-location portfolio;
- We created new and attractive packages of the most requested product configurations in our Cloud and Co-location portfolio to improve uptake and to simplify the sales process; and
- We bundled Connectivity and Cloud services to deliver enhanced value at a better price point.

ENHANCED MARKETING: Our strategic direction is clear, and our value proposition must resonate with customers. Work is underway to establish a clear positioning in the market to:

- Project a clear brand promise and narrative with increased marketing investment;
- Build a more powerful web-presence, able to fulfil the customers' increasingly digital journey to evaluate vendors (ultimately, this will lead to a full 'try and buy' capability for simple, lower-cost products); and
- Deploy effective demand and sales-generation programs that create greater awareness and consideration, and arm our sales teams with qualified leads.

EXPANDED SALES TEAM: We are investing in our sales organization to accelerate our growth efforts and to target the right customers with our offer:

- On-boarding new sales reps and leaders to increase the sales force by 25% - which was completed before the end of Q1 2017;
- Intensive sales training – both to improve performance and to ensure facility with the portfolio and our sales proposition; and
- Vertically-focused - subject matter expert - sales teams that foster strong client relationships.

AMAZON WEB SERVICES (AWS): To deliver innovation and value to our customers, TeraGo has selected AWS as its hyper-scale cloud infrastructure partner and has joined the AWS Partner Network (APN), allowing us to:

- Configure the right solutions for our customers' needs, which may include on-premise infrastructure, co-location infrastructure, private and public cloud;
- Support these services with migration and onboarding programs and the delivery of ongoing managed services – a market estimated to see a CAGR in excess of 20% over the coming years; and
- Provide enterprise class, resilient and redundant private interconnections between AWS infrastructure and the remainder of the client IT environment whether on-premise, colocation or private cloud on TeraGo infrastructure.

CUSTOMER SERVICE AND SUPPORT: We want to be recognized by our customers as their most trusted technology partner. New initiatives are under development to strengthen our relationships and transform customers into champions. This will enhance customer "stickiness", allow us to cross-sell new offers, and reduce overall customer churn as we target and acquire new customers.

This is significant progress in a short period of time. We have taken these steps and made the strategic investments that are critical to build the capabilities needed to both deepen relationships with existing customers and to capture new customers and new market share.

THE PATH FORWARD

As I noted earlier in my letter, this is an exciting time to be in this business. The market is expanding and our customers need our services and our support. The foundations being laid today will help to fuel our future growth. Disciplined execution will be the hallmark of TeraGo as we take our next steps forward to create greater value for customers and investors over the long-term.

We ended 2016 in a solid financial position. Our EBITDA showed growth and margins remained consistent in the low 30s which contributed to robust free cash flow in 2016. In addition, we bolstered our balance sheet with stronger cash and equivalents while diminishing our debt obligations. While Connectivity revenues showed a predicted decline of 9.9% in Q4 2016 compared to Q4 2015, we saw 13.3% growth in Cloud and Colocation over the same period.

As we advance, our strategic approach is intended to accelerate Cloud and Colocation growth by targeting the mid-market, where we have a strong competitive advantage, and to further slow

revenue erosion in our Connectivity business. Combined, this approach will drive meaningful and sustained revenue over the long term.

The work done over the past few months positions us well for this new, exciting journey. We are in build mode in 2017; making the changes, strategic decisions and investments necessary to drive better performance and growth over the long-term.

In closing, I would like to thank the employees of TeraGo for their dedication and efforts, and our customers across the country for the confidence they put in us every day.

Thank you.

(signed) "Antonio Ciciretto"

Antonio (Tony) Ciciretto
President & Chief Executive Officer

TERAGO INC.
MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL RESULTS FOR THE THREE MONTHS AND FISCAL YEAR ENDED DECEMBER 31, 2016 AND 2015

The following Management's Discussion and Analysis ("MD&A") is intended to help the reader understand the results of operations and financial condition of TeraGo Inc. All references in this MD&A to "TeraGo", the "Company", "we", "us", "our" and "our company" refer to TeraGo Inc. and its subsidiaries, unless the context requires otherwise. This MD&A is dated February 23, 2017 and should be read in conjunction with our audited consolidated financial statements for the year ended December 31, 2016 and the notes thereto. Additional information relating to TeraGo, including our most recently filed Annual Information Form ("AIF"), can be found on SEDAR at www.sedar.com and our website at www.terago.ca. For greater certainty, the information contained on our website is not incorporated by reference or otherwise into this MD&A. All dollar amounts included in this MD&A are in Canadian dollars unless otherwise indicated.

Certain information included herein is forward-looking and based upon assumptions and anticipated results that are subject to uncertainties. Should one or more of these uncertainties materialize or should the underlying assumptions prove incorrect, actual results may vary significantly from those expected. For a description of material factors that could cause our actual results to differ materially, see the "Forward-Looking Statements" section and the "Risk Factors" section in this MD&A. This MD&A also contains certain industry-related non-GAAP and additional GAAP measures that management uses to evaluate performance of the Company. These non-GAAP and additional GAAP measures are not standardized and the Company's calculation may differ from other issuers. See "Definitions – IFRS, Additional GAAP and Non-GAAP Measures".

FORWARD-LOOKING STATEMENTS

This MD&A includes certain forward-looking statements that are made as of the date hereof only and based upon current expectations, which involve risks and uncertainties associated with our business and the economic environment in which the business operates. All such statements are made pursuant to the 'safe harbour' provisions of, and are intended to be forward-looking statements under, applicable Canadian securities laws. Any statements contained herein that are not statements of historical facts may be deemed to be forward-looking statements. For example, the words *anticipate, believe, plan, estimate, expect, intend, should, may, could, objective* and similar expressions are intended to identify forward-looking statements. This MD&A includes, but is not limited to, forward looking statements regarding TeraGo's growth strategy, strategic plan, the growth in TeraGo's cloud and data centre businesses, retention campaign and initiatives to improve customer service, additional capital expenditures, investments in data centres, products and other IT services, expansion of network coverage, acquisitions and the integration of Codeninja Ltd. (doing business as "BoxFabric") and the hosting business assets acquired from AirVM Inc. into the Company (the "Hosting Business"). By their nature, forward-looking statements require us to make assumptions and are subject to inherent risks and uncertainties. We caution readers of this document not to place undue reliance on our forward-looking statements as a number of factors could cause actual future results, conditions, actions or events to differ materially from the targets, expectations, estimates or intentions expressed with the forward-looking statements. When relying on forward-looking statements to make decisions with respect to the Company, you should carefully consider the risks, uncertainties and assumptions, including the risk that TeraGo's growth strategy and strategic plan will not generate the result intended by management, cross-selling of TeraGo's cloud services may not succeed, retention efforts decreasing profit margins, opportunities for expansion and acquisition not being available or at unfavourable terms, the Company not being able to realize the anticipated benefits and synergies from combining and integrating BoxFabric and the Hosting Business into TeraGo's existing business and those risks set forth in the "Risk Factors" section of this MD&A and other uncertainties and potential events. In particular, if any of the risks materialize, the expectations, and the predictions based on them, of the Company may need to be re-evaluated. Consequently, all of the forward-looking statements in this MD&A are expressly qualified by these cautionary statements and other cautionary statements or factors contained herein, and there can be no assurance that the actual results or developments anticipated by the Company will be realized or, even if substantially realized, that they will have the expected consequences for the Company.

Except as may be required by applicable Canadian securities laws, we do not intend, and disclaim any obligation, to update or revise any forward-looking statements whether in words, oral or written as a result of new information, future events or otherwise.

OVERVIEW

Financial Highlights

- Total revenue decreased 3.4% to $14.6 million for the three months ended December 31, 2016 compared to $15.1 million for the same period in 2015. The decrease in revenue is primarily driven by lower connectivity revenue, partially offset by growth in cloud and colocation revenue. Cloud and colocation revenue increased 13.3% to $4.8 million compared to $4.2 million for the same period in 2015. The increase was driven by greater adoption of cloud services from new and existing customers as well as from the acquisition of the Hosting Business. The percentage of revenues from cloud and colocation of our total revenue have increased steadily quarter over quarter during 2016 (Q1 = 29.7%, Q2 = 30.0%, Q3 = 31.3% and Q4 = 32.9%).

  Total revenue increased 2.4% to $59.1 million for the twelve months ended December 31, 2016, compared to $57.7 million for the same period in 2015. On a year over year basis, the growth in the Company's cloud and colocation services were partially offset by the decline in connectivity revenue.

- Net income was $0.4 million for the three months ended December 31, 2016 compared to a net loss of $0.2 million for the same period in 2015. The increase in net income was primarily driven by lower finance costs, lower depreciation and amortization and lower stock-based compensation expense, partially offset by increased restructuring costs. For the twelve months ended December 31, 2016, net loss was $4.3 million compared to a net loss of $2.8 million for the same period in 2015.

- Adjusted EBITDA(1)(2) increased 0.5% to $4.89 million for the three months ended December 31, 2016 compared to $4.86 million for the same period in 2015. The increase in Adjusted EBITDA was primarily driven by lower salaries and related costs and other operating expenses. For the twelve months ended December 31, 2016, Adjusted EBITDA increased 2.9% to $18.9 million compared to $18.4 million for the same period in 2015.

Key Developments

- Effective January 1, 2017, the Company's wholly-owned subsidiaries, TeraGo Networks Inc. ("TeraGo Networks"), RackForce Networks Inc. ("RackForce"), RackForce Cloud Video Inc. and BoxFabric completed a vertical short-form amalgamation (the "Amalgamation"). The amalgamated corporation continues to carry on business as "TeraGo Networks Inc." and remains a wholly-owned subsidiary of TeraGo Inc. The Amalgamation was undertaken to simplify the Company's corporate structure and to obtain certain administrative and financial reporting efficiencies.

- On October 3, 2016, the Company announced that its Board of Directors had appointed Antonio (Tony) Ciciretto as President and Chief Executive Officer and replaced Stewart Lyons, outgoing President and CEO effective on that date. Mr. Ciciretto continues to serve as a member of the Board of Directors.

- On June 15, 2016 the Company was presented with the Canadian Telecommunications Employer of Choice (EOC) Recognition Award for 2016. This is the third consecutive year that TeraGo has been awarded this honour. The annual award is part of a national program dedicated to identifying, recognizing and promoting the best employers in the Canadian telecommunications industry.

- On February 24 2016, the Company announced that it will enhance its VMware-based cloud services across Canada. As part of its expanded collaboration with VMware, the Company will receive earlier access to new technology and platform updates from VMware, enabling it to accelerate the development and deployment of VMware vCloud powered services. The collaboration enables the Company's faster time-to-market delivery of enhanced VMware based cloud solutions.

- On January 18, 2016, TeraGo Networks was named in CIO Review's 20 Most Promising IT Infrastructure Solution Providers list for its expertise in delivering agility to manage data and IT Infrastructure. The positioning is based on the evaluation of TeraGo capability to efficiently address customers secure data flow and management requirements. The annual list of companies in the IT industry is selected by a panel of experts and members of CIO Review's editorial board to recognize and promote technology entrepreneurship.

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(1) Adjusted EBITDA is a Non-GAAP measure. See "Definitions - IFRS, Additional GAAP and Non-GAAP Measures.
(2) See "Adjusted EBITDA" for a reconciliation of net loss to Adjusted EBITDA

TERAGO OVERVIEW

TeraGo provides businesses across Canada and internationally with cloud, colocation and connectivity services, through nine (9) data centres as well as cloud Infrastructure as a Service ("IaaS") computing and storage solutions. With respect to the Company's connectivity services, it owns and operates a carrier-grade, Multi-Protocol Label Switching ("MPLS") enabled fixed wireless, IP communications network in Canada targeting businesses that require Internet access and data connectivity services.

The Company provides enterprise cloud services nationally and internationally to multiple high value enterprise customers across a variety of verticals, including secondary and post-secondary education, hospitals, federal and provincial governments and non-profit organizations. The Company specializes in managing enterprise cloud services including IaaS and Platform as a Service ("PaaS") with network. It currently has strategic relationships with several technology partners that give it access to certain products and solutions to provide enterprise cloud services.

The Company's subscription-based business model generates stable and predictable recurring revenue from cloud, colocation and connectivity services. The Company offers its connectivity services across Canada and its data and cloud services internationally. Once a customer is obtained, TeraGo's strategy is to generate incremental recurring revenue from that customer by: adding new customer locations, increasing service capacity supplied to existing locations, increasing data centre cabinet space and power and/or providing additional services, as applicable.

Cloud Services	Colocation Services	Connectivity Services
• Private and hybrid cloud • IaaS utility computing on virtual and dedicated compute platforms • High performance and secure data storage and archiving • Backup and recovery services for critical situations • Multiple managed services related to hybrid cloud offerings	• Colocation services in partial, full, or customized cabinets • Managed, Private Dedicated, and Co-location hosting services • Private Vaults protected with biometrics for maximum security • Other value added services such as hybrid cloud	• National high performance, scalable Internet access principally via wireless with fibre optic in selected strategic areas • Active redundancy capability with bundled connectivity solution • Unified communications • Managed network service

TERAGO'S BUSINESS MODEL

TeraGo's subscription-based business model generates stable and predictable recurring revenue from Internet, data, voice services, data centre services and cloud services.

TeraGo's customers typically sign one, two or three-year contracts. The majority of new customers sign contracts for three years or more. Services are billed monthly or quarterly over the term of the contract.

With its entry into data centre services and cloud services, TeraGo has built an operating platform to service the IT solutions sector. Cross selling opportunities to the customer base, while leveraging the Company's carrier grade network has augmented and diversified the Company's revenue base.

CLOUD SERVICES

TeraGo provides cloud services that seek to meet the complex and evolving IT needs of our customers. TeraGo provides IaaS for compute, storage, disaster recovery cloud solutions and other offerings either on a direct or indirect basis. These solutions allow the Company to compete in the cloud services market.

TeraGo offers customized cloud storage and compute offerings to customers across Canada. TeraGo cloud can offer a virtualized computing environment whereby customers can access on-demand computing power without the need to acquire and maintain expensive server equipment. TeraGo can also provide offsite cloud storage for key backup and disaster recovery situations, including utilizing partnerships with software and hardware vendors such as Veeam and Solidfire. The Company has strategic relationships and partnerships with technology leaders such as IBM, Cisco,

VMware, Microsoft, Mitel and others that gives it early access to intelligence, products and solutions to provide enterprise cloud services.

COLOCATION SERVICES

TeraGo provides data centre colocation services that protect and connect our customers' valuable information assets. Customers can provision computing equipment within shared partial cabinets or full, private cabinets, as well as customized caged space designed for their specific needs. TeraGo provides connectivity on redundant routes in and out of the facilities.

Hosting and colocation revenue is derived from set-up fees for new installations and monthly recurring charges based on the number of cabinets and/or the quantity of cage space, power requirements, managed services provided and Internet/data bandwidth requirements. Other services, such as disaster recovery services, are provided under custom contractual arrangements.

TeraGo also offers a variety of managed hosting solutions, which may require us to manage various aspects of a customer's hardware, software or operating systems in public or privately accessible environment. TeraGo offers disaster recovery services on a custom basis. This includes back-up office facilities that can be used in case of disaster. These facilities can be provisioned at the data centre location and provide customers with the capability to restore office functionality with direct access to their information located in the data centre.

Our network can provide these customers Internet and/or secure private virtual LAN connections between the data centre facility and the customer's office location(s).

Data centre services customers typically include national government agencies, financial services companies, cloud and data storage service providers, content and network service providers, and small and medium businesses which rely on TeraGo to store and manage their critical IT equipment and provide the ability to directly connect to the networks that enable our information-driven economy.

Data Centre Facilities

TeraGo's data centres provide data centre solutions, including colocation and disaster recovery, to a roster of small and medium-sized businesses, enterprises, public sector and technology service providers. TeraGo has approximately 60,000 square feet of data centre capacity in seven facilities across Canada:

Mississauga, Ontario
TeraGo operates a 10,000 square foot AT 101 SOC2 Type 2 certified data centre facility in Mississauga, Ontario that was previously managed by BlackBerry Limited and built to a tier 3 standard. This facility predominantly serves the Greater Toronto Area.

Vaughan, Ontario
TeraGo operates a 16,000 square foot AT 101 SOC2 Type 2 certified data centre facility in Vaughan, Ontario, serving the Greater Toronto Area. This data centre and its operations were purchased in May 2013 when the Company acquired Data Centres Canada Inc.

Kelowna, British Columbia
TeraGo operates its 18,000 square feet AT 101 SOC2 Type 2 certified data centre in Kelowna named the GigaCenter. The GigaCenter is built to a tier 3 standard and the location in Kelowna is considered ideal for a data centre as the region is considered a seismically stable geographic location, has a temperate climate and has a lower probability of both natural and man-made events that may be a risk.

Vancouver, British Columbia
TeraGo operates two AT 101 SOC2 Type 2 certified data centre facilities in downtown Vancouver. Its first facility, acquired in December 2013, is 5,000 square feet and is expandable to 7,000 square feet. The facility has redundant fibre facilities between the data centre and the 'telco hotel', 555 West Hastings, in downtown Vancouver. The second facility which was acquired in April 2014 is 7,000 square feet and is served by TeraGo's fiber optic lines. Both facilities are used to service the Greater Vancouver Area.

Winnipeg, Manitoba
TeraGo provides data centre services to its customers in central Canada through a data centre in Winnipeg. Colocation services, via the data centre facility, are provided through an agreement that TeraGo has with a local operator.

Ottawa, Ontario
TeraGo provides data centre services to its customers in Ottawa, Ontario through a Tier III AT 101 SOC 1 Type 2 certified data centre. Colocation services, via the data centre facility, are provided through an agreement that TeraGo has with a local operator.

St. Louis, Missouri, United States
TeraGo provides cloud services to its customers through a SSAE 16 (formerly SAS70) SOC 2 certified data centre in St. Louis, Missouri, United States pursuant to an agreement TeraGo has with a local operator.

Newport, Wales, United Kingdom
TeraGo provides cloud services to its customers through a Tier 3 designed data centre in Newport, Wales, United Kingdom pursuant to an agreement TeraGo has with a local operator.

CONNECTIVITY SERVICES

TeraGo owns and operates a carrier-grade Multi-Protocol Label Switching ("MPLS") enabled wireline and fixed wireless, Internet Protocol ("IP") communications network in Canada, providing businesses with high performance, scalable, and secure access and data connectivity services.

TeraGo's carrier grade IP communication network serves an important and growing demand among Canadian businesses for network access diversity by offering wireless services that are redundant to their existing wireline broadband connections.

TeraGo's IP network has been designed to eliminate single points of failure and the Company backs its services with customer service level commitments, including 99.9% service availability, industry leading mean time to repair, 24 x 7 telephone and e-mail access to technical support specialists.

TeraGo offers Canadian businesses high performance unlimited and usage-based dedicated Internet access with upload and download speeds from 5 megabits per second ("Mbps") up to 1 gigabit per second ("Gbps"). Unlike asymmetrical DSL services offered by many of our competitors, TeraGo provides services that are symmetrical, hence customers can have the same high speed broadband performance whether uploading or downloading. TeraGo enhances service performance by minimizing the number of networks between our customers and their audiences, using peering arrangements with multiple tier-one carriers to connect to the Internet.

To deliver its services, the Company has built and operates a carrier-grade, IP network, using licensed and license-exempt spectrum and fibre-optic wireline infrastructure that supports commercially available equipment.

The Company owns and controls a national MPLS distribution network from Vancouver to Montreal that aggregates customer voice and data traffic and interconnects where necessary with carrier diverse leased fiber optic facilities. Major Internet peering and core locations are centralized in Vancouver, Toronto and Seattle, although Internet access is also available in all regional markets for further redundancy.

TeraGo offers a range of diverse Ethernet-based services over a secured wireless connection to customer locations up to 20 kilometres from a hub (provided line of sight or wireline networks exist) or through a fibre optic connection.

Quality of Service Capabilities

TeraGo's MPLS network, including key high traffic hub sites, is equipped with Quality of Service ("QoS") capabilities to improve performance and traffic management. All of TeraGo's major national markets are end-to-end QoS enabled providing the foundation to support voice traffic and other potential future applications.

Radio Spectrum

24-GHz and 38-GHz Wide-area Licences
The Company owns a national spectrum portfolio of 24-GHz and 38-GHz wide-area spectrum licences which covers regions across Canada, including 1,160 MHz in Canada's 6 largest cities. This spectrum is used for: point-to-point and point-to-multipoint microwave radio deployments; connecting core hubs together to create a wireless backbone where appropriate (often in a ring configuration to avoid points of failure); and in the access network or "last mile" to deliver high capacity (speeds of 10 to 1,000 Mbps) Ethernet-based links for business, government and cellular backhaul.

For further details on licensed spectrums, please refer to the Company's 2016 AIF**.**

Voice Services

TeraGo provides a number of unified communications services and is approved by the Canadian Radio-television and Telecommunications Commission ("CRTC") to offer voice services as a Type IV competitive local exchange carrier ("CLEC"). TeraGo provides businesses with a cost effective, flexible and high quality connection from their private branch exchange (PBX) to the public switched telephone network (PSTN). TeraGo's service provides features and capabilities generally consistent with those provided by incumbent local exchange carriers ("ILECs"), while offering greater value for our customers.

SELECTED ANNUAL INFORMATION

The following table displays a summary of our Consolidated Statements of Comprehensive Earnings (Loss) for the three months ended December 31, 2016 and 2015 and the years ended December 31, 2016, 2015 and 2014 and a summary of select Balance Sheet data as at December 31, 2016, 2015 and 2014.

(in thousands of dollars, except with respect to earnings (loss) per share)	Three months ended December 31		Years ended December 31		
	2016	**2015**	**2016**	**2015**	**2014**
Revenue					
Cloud and colocation revenue	$ 4,798	4,235	$ 18,296	13,166	3,402
Connectivity revenue	9,795	10,867	40,790	44,554	47,827
Total Revenue	14,593	15,102	59,086	57,720	51,229
Expenses					
Cost of services	3,322	3,420	13,477	13,159	10,102
Salaries and related costs	4,660	4,707	21,195	20,587	20,747
Other operating expenses	2,239	2,667	10,845	10,062	9,003
Amortization of intangible assets	792	1,016	3,529	3,697	2,781
Depreciation of network assets, property and equipment	2,859	2,934	11,796	11,400	10,479
	13,872	14,744	60,842	58,905	53,112
Earnings (loss) from operations	721	358	(1,756)	(1,185)	(1,883)
Foreign exchange loss	(2)	(11)	16	(171)	(84)
Finance costs	(379)	(544)	(1,882)	(2,624)	(1,990)
Finance income	-	11	8	37	30
Earnings (loss) before income taxes	340	(186)	(3,614)	(3,943)	(3,927)
Income taxes					
Income tax recovery (expense)	15	(4)	(700)	1,133	-
Net earnings (loss) and comprehensive earnings (loss)	$ 355	(190)	$ (4,314)	(2,810)	(3,927)
Deficit, beginning of year	(63,498)	(58,639)	(58,829)	(56,019)	(52,092)
Deficit, end of year	$ (63,143)	(58,829)	$ (63,143)	(58,829)	(56,019)
Basic earnings (loss) per share	$ 0.02	(0.01)	$ (0.30)	(0.22)	(0.34)
Diluted earnings (loss) per share	$ 0.02	(0.01)	$ (0.30)	(0.22)	(0.34)
Basic weighted average number of shares outstanding	14,223	14,065	14,177	13,069	11,588
Diluted weighted average number of shares outstanding	14,230	14,065	14,177	13,069	11,588

Selected Balance Sheet Data	As at December 31		
	2016	**2015**	**2014**
Cash and cash equivalents	$ 13,034	$ 13,066	$ 2,866
Short term investments	$ -	$ -	$ -
Accounts receivable	$ 3,673	$ 3,306	$ 2,908
Prepaid expenses and other assets	$ 3,150	$ 3,351	$ 2,431
Network assets, property and equipment	$ 44,161	$ 48,520	$ 41,774
Total Assets	$ 102,837	$ 110,002	$ 69,561
Accounts payable and accrued liabilities	$ 11,027	$ 9,128	$ 7,401
Long-term debt	$ 40,778	$ 45,781	$ 18,794
Other long-term liabilities	$ 1,567	$ 2,163	$ 1,382
Shareholders' equity	$ 48,648	$ 52,215	$ 41,413

RESULTS OF OPERATIONS

Comparison of the three and twelve months ended December 31, 2016 and 2015
(in thousands of dollars, except with respect to gross profit margin and earnings per share)

	Three months ended December 31		Twelve months ended December 31	
	2016	**2015**	**2016**	**2015**
Financial				
Cloud and colocation revenue	$ 4,798	$ 4,235	$ 18,296	$ 13,166
Connectivity revenue	$ 9,795	$ 10,867	$ 40,790	$ 44,554
Total Revenue	$ 14,593	$ 15,102	$ 59,086	$ 57,720
Cost of Services[(1)]	$ 3,322	$ 3,420	$ 13,477	$ 13,159
Gross profit margin [(1)]	77.2%	77.4%	77.2%	77.2%
Adjusted EBITDA[(1) (2)]	$ 4,889	$ 4,863	$ 18,941	$ 18,403
Income tax recovery (expense)	$ 15	$ (4)	$ (700)	$ 1,133
Net loss	$ 355	$ (190)	$ (4,314)	$ (2,810)
Basic loss per share[(3)]	$ 0.02	$ (0.01)	$ (0.30)	$ (0.22)
Diluted loss per share	$ 0.02	$ (0.01)	$ (0.30)	$ (0.22)

(1) See "Definitions - IFRS, Additional GAAP and Non-GAAP Measures"

(2) See "Adjusted EBITDA" for a reconciliation of net loss to Adjusted EBITDA

(3) The comparative basic and diluted weighted average number of shares outstanding for the year ended December 31, 2015 have been corrected to 13,069 shares outstanding, due to an immaterial arithmetic error in the prior year financial statements. As a result, the basic and diluted earnings per share was adjusted from ($0.23) to ($0.22).

Refer to "Definitions – IFRS, Additional GAAP and Non-GAAP Measures" for a description of the components of relevant line items below.

Revenue

Total revenue decreased 3.4% to $14.6 million for the three months ended December 31, 2016 compared to $15.1 million for the same period in 2015. Total revenue increased 2.4% to $59.1 million for the twelve months ended December 31, 2016, compared to $57.7 million for the same period in 2015.

Cloud and colocation revenue

For the three months ended December 31, 2016, cloud and colocation revenue increased 13.3% to $4.8 million compared to $4.2 million for the same period in 2015. The increase was driven by greater adoption of cloud services from new and existing customers as well as from the acquisition of the Hosting Business. For the twelve months ended December 31, 2016, cloud and colocation revenue increased 39.0% to $18.3 million compared to $13.2 million for the same period in 2015. The increase was driven by the factors described above, as well as the acquisitions of RackForce, BoxFabric and the Hosting Business. The percentage of revenues from cloud and colocation of our total revenue have increased steadily quarter over quarter during 2016 (Q1 = 29.7%, Q2 = 30.0%, Q3 = 31.3% and Q4 = 32.9%).

Connectivity revenue

Connectivity revenues were impacted by a variety of factors, including regional economic difficulties, the company moving away from maintaining its lowest value customers, certain customers renewing long term contracts at lower current market rates and lower usage revenues as certain customers have shifted to unlimited usage plans.

Cost of services

For the three months ended December 31, 2016, cost of services decreased 2.9% to $3.3 million compared to $3.4 million for the same period in 2015. The decrease was primarily driven by savings in local loop and transit costs. For the twelve months ended December 31, 2016, cost of services increased to $13.5 million compared to $13.2 million for the same period in 2015. The increase is mainly due to costs associated with owning RackForce, BoxFabric and the Hosting Business, partially offset by the synergies noted above.

Salaries and related costs and other operating expenses ("SG&A")
For the three months ended December 31, 2016, SG&A decreased to $6.9 million compared to $7.4 million for the same period in 2015. The decrease was primarily driven by lower personnel related expenses, an adjustment to an onerous contract provision related to a data centre due to the increasing number of customers served, and lower legal fees, partially offset by increased restructuring, acquisition-related and integration costs, including those associated with the departure of the former COO. For the twelve months ended December 31, 2016, SG&A increased to $32.0 million compared to $30.6 million for the same period in 2015. The increase was primarily driven by restructuring charges for the former President and CEO and VP of Marketing, and due to costs associated with owning RackForce, BoxFabric and the Hosting Business.

Adjusted EBITDA(1)
For the three months ended December 31, 2016, Adjusted EBITDA(1) increased 0.5% to $4.89 million compared to $4.86 million for the same period in 2015. The increase in Adjusted EBITDA(1) was primarily driven by lower salaries and related costs and other operating expenses offset by decreased connectivity revenue. For the twelve months ended December 31, 2016, Adjusted EBITDA(1) increased 2.9% to $18.9 million compared to $18.4 million for the same period in 2015. The increase was driven by the acquisitions of RackForce, BoxFabric and the Hosting Business, partially offset by the introduction of costs associated from the acquisitions and the factors described above.

The table below reconciles net loss to Adjusted EBITDA(1) for the three and twelve months ended December 31, 2016 and 2015.

(in thousands of dollars)	**Three months ended December 31**		**Twelve months ended December 31**	
	2016	**2015**	**2016**	**2015**
Net earnings (loss) for the period	$ 355	$ (190)	$ (4,314)	$ (2,810)
Foreign exchange loss (gain)	2	11	(16)	171
Finance costs	379	544	1,882	2,624
Finance income	-	(11)	(8)	(37)
Income tax (recovery) expense	(15)	4	700	(1,133)
Earnings (loss) from operations	721	358	(1,756)	(1,185)
Add:				
Depreciation of network assets, property and equipment and amortization of intangible assets	3,651	3,950	15,325	15,097
Loss (gain) on disposal of network assets	85	135	397	266
Stock-based compensation expense	16	266	866	1,272
Restructuring, acquisition-related, integration costs and other	416	154	4,109	2,953
Adjusted EBITDA(1)	$ 4,889	$ 4,863	$ 18,941	$ 18,403

(1) See "Definitions - IFRS, Additional GAAP and Non-GAAP Measures"

Finance costs
For the three months ended December 31, 2016, finance costs decreased to $0.4 million compared to $0.5 million for the same period in 2015. For the twelve months ended December 31, 2016, finance costs decreased to $1.9 million compared to $2.6 million for the same period in 2015. The decrease in both periods was driven by the mark to market impact of revaluing the Company's interest rate swap contract on the drawn credit facility.

Income tax expense
For the three months ended December 31, 2016, there was an income tax recovery of $15 thousand compared to an income tax expense of $4 thousand for the same period in 2015. For the twelve months ended December 31, 2016, income tax expense increased to $0.7 million compared to a recovery of $1.1 million for the same period in 2015 due to changes in the anticipated recovery of deferred tax assets in the near term.

Depreciation and amortization
For the three months ended December 31, 2016, depreciation of network assets, property and equipment and amortization of intangibles decreased by $0.3 million compared to the same period in 2015. For the twelve months ended December 31, 2016, depreciation of network assets, property and equipment and amortization of intangibles increased to $15.3 million compared to $15.1 million for the same period in 2015. The increase is mainly attributed to the depreciation and amortization of RackForce acquired intangibles and cloud and data centre infrastructure for all of fiscal 2016 compared to nine months in 2015.

Net loss
For the three months ended December 31, 2016, net income was $0.4 million compared to a net loss of $0.2 million for the same period in 2015. The increase in net income was primarily driven by lower finance costs, lower depreciation and amortization and lower stock-based compensation expense, partially offset by increased restructuring costs. For the twelve months ended December 31, 2016, net loss was $4.3 million compared to a net loss of $2.8 million for the same period in 2015. Net loss was negatively impacted compared to the prior period by increased restructuring, acquisition-related and integration costs, and a write-off of deferred tax assets, partially offset by revenue growth in the cloud and colocation services associated with the RackForce, BoxFabric and the Hosting Business acquisitions.

Summary of Quarterly Results

All financial results are in thousands, with the exception of earnings per share

		Q4-16	Q3-16	Q2-16	Q1-16	Q4-15	Q3-15	Q2-15	Q1-15
Revenue	$	14,593	14,780	14,784	14,929	15,102	15,272	15,110	12,236
Gross Profit Margin % (1)		77.2%	77.5%	77.3%	76.8%	77.4%	76.3%	76.6%	78.9%
Adjusted EBITDA (1)	$	4,889	4,481	4,895	4,676	4,863	5,313	4,529	3,696
Net earnings (loss)	$	355	(3,454)	(395)	(820)	(190)	(432)	(2,176)	(16)
Basic earnings (loss) per share	$	0.02	(0.24)	(0.03)	(0.06)	(0.01)	(0.03)	(0.17)	(0.00)
Diluted earnings (loss) per share	$	0.02	(0.24)	(0.03)	(0.06)	(0.01)	(0.03)	(0.17)	(0.00)
Basic weighted average number of shares outstanding		14,223	14,190	14,159	14,135	14,065	13,966	12,476	11,734
Diluted weighted average number of shares outstanding		14,230	14,190	14,159	14,135	14,065	13,966	12,476	11,734

(1) See "Definitions - IFRS, Additional GAAP and Non-GAAP Measures" for descriptions of Gross profit margin % and Adjusted EBITDA

Seasonality
The Company's net customer growth, with respect to its connectivity business, is typically impacted adversely by weather conditions as the majority of new customer locations require the installation of rooftop equipment. Typically, harsher weather in the first quarter of the year results in a reduction of productive installation days.

The Company's cash flow and earnings are typically impacted in the first quarter of the year due to several annual agreements requiring payments in the first quarter including annual rate increases in long-term contracts and the restart on January 1st of payroll taxes and other levies related to employee compensation.

LIQUIDITY AND CAPITAL RESOURCES

TeraGo has historically financed its growth and operations through cash generated by operations, the issuance of equity securities and long-term debt.

The table below is a summary of cash inflows and outflows by activity.

(in thousands of dollars)	Three months ended December 31		Twelve months ended December 31	
	2016	2015	2016	2015
Statement of Cash Flows Summary				
Cash inflows and (outflows) by activity:				
Operating activities	$ 5,067	5,212	$ 16,358	15,686
Investing activities	(2,312)	(1,307)	(9,565)	(41,089)
Financing activities	(1,614)	(1,482)	(6,825)	35,603
Net cash inflows (outflows)	1,141	2,423	(32)	10,200
Cash and cash equivalents, beginning of period	11,893	10,643	13,066	2,866
Cash and cash equivalents, end of period	$ 13,034	13,066	$ 13,034	13,066

Operating Activities

For the three months ended December 31, 2016, cash generated from operating activities was $5.1 million compared to cash generated of $5.2 million for the same period in 2015. The decrease in cash generated is due to changes in working capital. For the twelve months ended December 31, 2016, cash generated from operating activities was $16.4 million compared to cash generated of $15.7 million for the same period in 2015 principally related to changes in working capital.

Investing Activities

For the three months ended December 31, 2016, cash used in investing activities was $2.3 million compared to cash used of $1.3 million for the same period in 2015. The increase in cash used in investing activities is due to higher capital expenditures related to provisioning customers. For the twelve months ended December 31, 2016, cash used in investing activities was $9.6 million compared to cash used of $41.1 million for the same period in 2015. The year ended December 31, 2015 included $31.0 million for the acquisition of RackForce.

Financing Activities

For the three months ended December 31, 2016, cash used from financing activities was $1.6 million compared to cash used of $1.5 million for the same period in 2015. For the twelve months ended December 31, 2016, cash used from financing activities was $6.8 million compared to cash generated of $35.6 million for the same period in 2015. The increase in cash used for financing for the three months ended December 31, 2016 is due to a reduction of proceeds from exercised options pursuant to the Company's stock option plan, which are partially offset by less interest and principal repayments. The increase in cash used from financing activities for the twelve months ended December 31, 2016 is mainly due to higher cash proceeds received for the same period in 2015 from the amended credit facility to finance the acquisition of RackForce and an equity offering.

Capital Resources

As at December 31, 2016, the Company had cash and cash equivalents of $13.0 million and access to the $34.3 million undrawn portion of its $85.0 million credit facilities.

The Company anticipates incurring additional capital expenditures for the purchase and installation of network, data centre and cloud assets, systems and processes upgrades and customer premise equipment. As economic conditions warrant, the Company may expand its network coverage into new Canadian markets using wireless or fibre optics and making additional investments in data centres, cloud and other IT services through acquisitions or expansion.

Management believes the Company's current cash, anticipated cash from operations, access to the undrawn portion of debt facilities and its access to additional financing in the form of debt or equity will be sufficient to meet its working capital and capital expenditure requirements for the foreseeable future.

Term Debt Facility
In June 2014, the Company entered into an agreement with a syndicate led by the National Bank of Canada ("NBC") to provide a $50.0 million credit facility that is principally secured by a general security agreement over the Company's assets.

In March 2015, the Company entered into an amended agreement with a syndicate led by NBC that increases the credit facility by $35.0 million ($30.0 million increase to the term debt facility and $5.0 million increase to the revolving facility) and extended the term from June 6, 2017 to June 30, 2018. Other terms are substantially consistent with the existing credit facilities.

The total $85.0 million facility that matures June 30, 2018 is made up of the following:

- $10.0 million revolving facility which bears interest at prime plus a margin percent. As of December 31, 2016, $nil amount is outstanding (December 31, 2015 - $nil). Letters of credit outstanding under the facility totaled $655 thousand as of December 31, 2016 (December 31, 2015 - $655 thousand).

- $50.0 million term facility which bears interest at prime or Banker's Acceptance (at the Company's option) plus a margin percent and is repayable in quarterly principal installments of $1.3 million starting June 30, 2015. This facility was fully drawn upon signing the amended agreement.

  On December 31, 2016, $41.1 million of the term facility principal balance outstanding was in a Banker's Acceptance and the remaining $150 thousand was at a floating rate. In 2015, the Company entered into amended interest rate swap contracts that matures June 29, 2018. The interest rate on the Banker's Acceptance at December 31, 2016 was 3.99%. The interest rate swap contract has not been designated as a hedge and will be marked-to-market each quarter. The fair value of the interest rate swap contract at December 31, 2016 was a liability of $261 thousand (December 31, 2015 – $612 thousand) and is recorded in other long-term liabilities, with a corresponding charge for the change in fair value recorded in finance costs.

  As at December 31, 2016, the Company prepaid interest in the amount of $353 thousand which represents the net settlement of the Banker's Acceptance and is recorded as a reduction in the carrying value of the debt.

- $25.0 million available for funding acquisitions and will bear interest at prime or Banker's Acceptance (at the Company's option) plus a margin percent and is repayable in quarterly principal installments of 2.5% of the aggregate amount outstanding. As of December 31, 2016, this facility remains undrawn.

The financing fees have been deferred and amortized using the effective interest method over the term of the facility.

The NBC facility is subject to certain financial and non-financial covenants which the Company is in compliance with at December 31, 2016. Under this facility, the Company is also subject to a cash flow sweep that could accelerate principal repayments based on a detailed calculation outlined by NBC not later than 120 days after the end of each fiscal year.

Equity Offering
On June 11, 2015, the Company completed an equity offering to issue and sell 1,755 common shares for gross proceeds of $10.0 million (the "Offering"). Proceeds net of commissions, legal, accounting and listing fees were $9.2 million. The Offering was carried out pursuant to an underwriting agreement with a syndicate of underwriters led by National Bank Financial Inc. and TD Securities Inc. and included Cormark Securities Inc., PI Financial Corp. and RBC Capital Markets.

The Company allocated $9.2 million of the intended use of net proceeds from the equity offering as follows:

Intended Use of Net Proceeds	Allocation	Use of Net Proceeds as at December 31, 2016
a) Fund its continued growth strategy, which is expected to include potential strategic acquisitions	$4.0 million	$2.4 million
b) Fund operational efficiency initiatives	$3.2 million	$0.6 million
c) Invest in new product development activities, specifically in the cloud and data centre segments	$2.0 million	$0.3 million

As of December 31, 2016, $3.3 million of the net proceeds from the equity offering were used. The Company's intended use of these proceeds has not changed.

Contractual Obligations
The Company is committed to leases for premises, office equipment, network real estate access, automobiles, telecommunication facilities and radio spectrum licenses. Annual minimum payments over the next five years and thereafter are as follows:

		Amount
2017	$	11,297
2018		8,938
2019		7,281
2020		4,261
2021		3,541
Thereafter		2,321
	$	37,639

Off-balance Sheet Arrangements
As of December 31, 2016, the Company had no off-balance sheet arrangements apart from operating leases noted above.

Transactions with Related Parties
Two former Directors of the Company, who retired effective June 23, 2016, also served as Chairman of the Board and a Director of a customer of the Company. Revenue from this customer for the year ended December 31, 2016 and 2015 was $40 thousand and $79 thousand, respectively. Accounts receivable from this customer as at December 31, 2016 and 2015 was nil and $3 thousand, respectively.

The terms governing these related party transactions are consistent with those negotiated on an arm's length basis with non-related parties.

Share Capital
TeraGo's authorized share capital consists of an unlimited number of Common Shares, an unlimited number of Class A Non-Voting Shares and two Class B Shares. A detailed description of the rights, privileges, restrictions and conditions attached to the authorized shares is included in the Company's 2015 Annual Information Form, a copy of which can be found on SEDAR at www.sedar.com.

As of February 23, 2017, there were 14,258 thousand Common Shares issued and outstanding and two Class B Shares issued and outstanding. In addition, as of February 23, 2017, there were 660 thousand Common Shares issuable upon exercise of TeraGo stock options.

Financial Instruments
The Company initially measures financial instruments at fair value. Transaction costs that are directly attributable to the issuance of financial assets or liabilities are accounted for as part of the carrying value at inception (except for transaction costs related to financial instruments recorded as FVTPL financial assets which are expensed as incurred), and are recognized over the term of the assets or liabilities using the effective interest method.

Subsequent measurement and treatment of any gain or loss is recorded as follows:

(i) Financial assets and financial liabilities at FVTPL are measured at fair value at the balance sheet date with any gain or loss recognized immediately in net loss. Interest and dividends earned from financial assets are also included in net loss for the period.
(ii) Loans and receivables are measured at amortized cost using the effective interest method. Any gains or losses are recognized in net loss for the period.
(iii) Other financial liabilities are measured at amortized cost using the effective interest method. Any gains or losses are recognized in net loss for the period.

The following is a summary of the Company's significant categories of financial instruments as at December 31, 2016:

Impairment of Financial Assets
A financial asset carried at amortized cost is considered impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flow of that asset that can be estimated reliably. An

impairment loss is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate.

In assessing impairment, the Company uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends. Losses are recognized in the consolidated statements of loss and reflected in an allowance account against the financial asset.

Loans and receivables
Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets currently are comprised of cash and cash equivalents, accounts receivable and restricted cash.

(i) ***Cash and Cash Equivalents and restricted cash***
Cash and cash equivalents consists of bank balances, cash on hand, demand deposits that can be withdrawn without penalty and short-term, highly liquid securities such as debt securities with an initial maturity date of not more than three months from the date of acquisition, that can readily be converted into known amounts of cash and are subject to an insignificant risk of change in value. Bank overdrafts that are repayable upon demand and form an integral part of the Company's cash management are included as a component of cash and cash equivalents. Cash and cash equivalents and restricted cash are carried at amortized cost.

(ii) ***Accounts Receivable***
Accounts receivable are measured at the amount the item is initially recognized. The allowance for doubtful accounts is based on the Company's assessment of the collectability of outstanding trade receivables. The evaluation of collectability of customer accounts is done on an individual account basis. If, based on an evaluation of accounts, it is concluded that it is probable that a customer will not be able to pay all amounts due, an expected impairment loss is recognized. Recoveries are only recorded when objective verifiable evidence supports the change in the original allowance. Changes in the carrying amount of the allowance account are recognized in the statement of comprehensive loss for the period.

Other financial liabilities
The Company recognizes debt securities issues and subordinated liabilities on the date that they originated. All other financial liabilities are recognized initially on the date that the Company becomes a party to the contractual provisions. The Company has the following non-derivative financial liabilities: current and long-term debt, accounts payable and accrued liabilities, and current portion and long-term portion of other long term liabilities.

Such liabilities are recognized initially at fair value less any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortized cost using the effective interest method.

Interest on loans and borrowings is expensed as incurred unless capitalized for qualifying assets in accordance with IAS 23, Borrowing Costs. Loans and borrowings are classified as a current liability unless the Company has an unconditional right to defer settlement for at least 12 months after the end of the year.

Derivative instruments
The Company uses an interest rate swap contract to manage the risk associated with the fluctuations of interest rates on its long-term debt. Management does not apply hedge accounting on the interest rate swap contract. As a result, the interest rate swap contract is marked to market each period, resulting in a gain or loss in net loss for the year.

Financial Instrument Risks

Fair value of financial instruments
The Company has determined the estimated fair values of its financial instruments based on appropriate valuation methodologies. Where quoted market values are not readily available, the Company may use considerable judgment to develop estimates of fair value. Accordingly, any estimated values are not necessarily indicative of the amounts the Company could realize in a current market exchange and could be materially affected by the use of different assumptions or methodologies. The Company classifies its fair value measurements within a fair value hierarchy,

which reflects the significance of the inputs used in making the measurements as defined in IFRS 7 – Financial Instruments – Disclosures.

Level 1 - Unadjusted quoted prices in active markets for identical assets or liabilities;
Level 2 - Inputs other than quoted prices included in Level 1, that are observable for the asset or liability, either directly or indirectly; and
Level 3 - Unobservable inputs for the asset or liability which are supported by little or no market activity

The fair values of cash and cash equivalents, short-term investments and restricted cash, which are primarily money market and fixed income securities, are based on quoted market values. The fair values of short-term financial assets and liabilities, including accounts receivable, accounts payable and accrued liabilities, as presented in the consolidated statements of financial position, approximate their carrying amounts due to their short-term maturities. The fair value of long-term debt approximates its carrying value because management believes the interest rates approximate the market interest rate for similar debt with similar security. The fair value of our interest rate swap contract is based on broker quotes and therefore, these contracts are measured using Level 2 inputs. Similar contracts are traded in an active market and the quotes reflect the actual transactions in similar instruments.

Credit risk
The Company's cash and cash equivalents and restricted cash subject the Company to credit risk. The Company maintains cash and investment balances at Tier 1 Canadian financial institutions. The Company's maximum exposure to credit risk is limited to the amount of cash and cash equivalents.

Credit risk related to our interest rate swap contract arises from the possibility that the counter party to the agreement may default on their obligation. The Company assesses the creditworthiness of the counterparty to minimize the risk of counterparty default. The interest rate swap is held by National Bank Financial.

The Company, in the normal course of business, is exposed to credit risk from its customers and the accounts receivable are subject to normal industry risks. The Company attempts to manage these risks by dealing with credit worthy customers. If available, the Company reviews credit bureau ratings, bank accounts and industry references for all new customers. Customers that do not have this information available are typically placed on a pre-authorized payment plan for service or provide deposits to the Company. This risk is minimized as the Company has a diverse customer base located across various provinces in Canada.

As at December 31, 2016 and 2015, the Company had no material past due trade accounts receivable.

Interest rate risk
The Company is subject to interest rate risk on its cash and cash equivalents and long-term debt. The Company is exposed to interest rate risk on its operating line of credit since the interest rates applicable are variable and is, therefore, exposed to cash flow risks resulting from interest rate fluctuations. As at December 31, 2016, the operating line of credit balance was $nil. The drawn term facility as at December 31, 2016 was $41.3 million, $41.1 million of which was held in a Bankers Acceptance. In 2015, the Company entered into amended interest rate swap contracts that matures June 29, 2018. The interest rate on the Banker's Acceptance at December 31, 2016 was 3.99%. The remaining $150 thousand drawn under this facility bears interest for the period at prime rate plus a margin.

Liquidity risk
The Company believes that its current cash and cash equivalents and anticipated cash from operations will be sufficient to meet its working capital and capital expenditure requirements for the foreseeable future. As at December 31, 2016, the Company had cash and cash equivalents of $13.0 million. The Company has access to the $34.3 million undrawn portion of its $85,000 credit facilities after consideration of outstanding letters of credit.

SIGNIFICANT ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Estimates and assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Key areas of estimation and information about critical judgments in applying accounting policies that have the most significant effect on amounts recognized in the consolidated financial statements are:

(i) *Estimates of useful lives of network assets, property and equipment and intangible assets:* Management's judgment involves consideration of intended use, industry trends and other factors in determining the expected useful lives of depreciable assets, to determine depreciation methods, the asset's residual value and whether an asset is a qualifying asset for the purposes of capitalizing borrowing costs.

(ii) *Capitalization of costs:*
Judgments and estimates are used in assessing the direct labour and other costs capitalized to network assets, property and equipment.

(iii) *Cash generating units:*
Judgment is required to assess the Company's determination of cash generating units for the purpose of impairment testing.

(iv) *Impairment of non-financial assets:*
The process to calculate the recoverable amount of our cash generating unit requires use of valuation methods such as the discounted cash flow method which uses assumptions of key variables including future cash flows, discount rate and terminal growth rates.

(v) *Allowance for doubtful accounts:*
In developing the estimates for an allowance against existing receivables, the Company considers general and industry economic and market conditions as well as credit information available for the customer and the aging of the account. Changes in the carrying amount due to changes in economic and market conditions could significantly affect the loss for the period.

(vi) *Stock-based compensation:*
Estimating fair value for stock-based payments requires determining the most appropriate valuation model for a grant, which is dependent on the terms and conditions of the grant. In valuing stock options, the Company uses the Black-Scholes option pricing model. Several assumptions are used in the underlying calculation of fair values of the Company's stock options using the Black-Scholes option pricing model including the expected life of the option, risk-free interest rate and volatility of the underlying stock.

(vii) *Business combination:*
The amount of goodwill initially recognized as a result of a business combination, the fair value estimate of any contingent consideration and the determination of the fair value of the identifiable assets acquired and the liabilities assumed is based, to a considerable extent, on management's estimate of future cash flows expected to be derived from the assets acquired.

(viii) *Income taxes:*
A deferred tax asset is recognized for unused losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable income will be available against which they can be utilized. Significant estimates are required in evaluating the recoverability of deferred tax assets. The Company's assessment is based on existing tax laws, estimates of future profitability and tax planning strategies.

(ix) *Provisions:*
Judgment is required to assess the likelihood of an outflow of the economic benefits to settle contingencies, such as litigations or decommissioning and restoration obligations, which may require a liability to be recognized. Significant judgments include assessing estimates of future cash flows, selection of discount rates and the probability of the occurrence of future events.

RISK FACTORS

TeraGo is exposed to a number of risks and uncertainties that are common to other companies engaged in the same or similar businesses. The following is a summary of the material risks that could significantly affect the financial condition, operating results or business of TeraGo.

Revenues and Operating Results Can Fluctuate
Our revenue in past periods may not be indicative of future performance from quarter to quarter or year to year. In addition, our operating results may not follow any past trends. The factors affecting our revenue and results, many of which are outside of our control, include:

- competitive conditions in the industry, including strategic initiatives by us or our competitors, new services, service announcements and changes in pricing policy by us or our competitors;
- market acceptance of our services;
- timing and contractual terms of orders for our services, which may delay the recognition of revenue;
- the discretionary nature of purchase and budget cycles of our customers and changes in their budgets for, and timing of, services orders;
- strategic decisions by us or our competitors, such as acquisitions, divestitures, spin-offs, joint ventures, strategic investments or changes in business strategy;
- general weakening of the economy resulting in a decrease in the overall demand for telecommunications, data centre, cloud or IT services or otherwise affecting the capital investment levels of medium-sized and enterprise businesses;
- timing of the development of new service offerings;
- no assurance that the Company's current and future competitors will not be able to develop data centre or cloud services or other infrastructure expertise comparable or superior to those developed by the Company or to adapt more quickly than the Company to new technologies, evolving industry standards or customer requirements;
- seasonal factors which may cause certain cloud service customers to increase or decrease their usage based services

Transition of the Company to a Multi-Product IT Services Company
In the past, the core business of the Company was to provide internet access services. The Company has recently transitioned to a multi-product IT services company focused on the management of its customer's data flow. In doing so, TeraGo is offering colocation services through its data centres and is offering cloud storage and cloud computing services. If TeraGo is unable to execute on its new business strategy and to grow the business, either as a result of the risks identified in this section or for any other reason, the business, prospects, financial condition and results of operations will be materially and adversely affected.

Integration and Anticipated Benefits Pursuant to Recent Acquisitions
On March 27, 2015, the Company completed the acquisition of RackForce, on September 18, 2015, the Company completed the acquisition of BoxFabric and on May 26, 2016 the Company completed the acquisition of the Hosting Business (collectively the "Acquisitions"). The Company may not be able to fully realize the anticipated future benefits and synergies of the Acquisitions on a timely basis or at all. The Acquisitions involve challenges and risks, including risks that the transactions do not advance TeraGo's business strategy or that the Company will not realize a satisfactory return. The potential failure of the due diligence processes to identify significant problems, liabilities or other shortcomings or challenges with respect to assets of RackForce, BoxFabric and the Hosting Business including customer contracts, condition of the equipment acquired, intellectual property, revenue recognition or other accounting practices, taxes, corporate governance and internal controls, regulatory compliance, employee, supplier or partner disputes or issues and other legal and financial contingencies could decrease or eliminate the anticipated benefits and synergies of the Acquisitions and could negatively affect the Company's future business and financial results.

The overall success of the Acquisitions will depend, in part, on the Company's ability to realize the anticipated benefits and synergies from combining and integrating the RackForce, BoxFabric and the Hosting Business businesses into TeraGo's existing business. In particular, the Company's offering of cloud services is relatively new and the limited experience of management in providing cloud services prior to the Acquisitions may limit the full benefits or continued growth of such business. Integration of RackForce, BoxFabric and the Hosting Business requires significant management attention and expansion of TeraGo's staff in operations, marketing, sales and general and administrative functions. The Company may have difficulties in the integration of the acquired company's departments, systems, including accounting, human resource and other administrative systems, technologies, books and records, and procedures, as well as in maintaining uniform standards, controls, including internal control over financial reporting

required by Canadian securities laws and related procedures and policies. If we cannot integrate the Acquisitions successfully, it could have a material adverse impact on our business, financial condition and results of operations.

As part of the Company's business strategy, TeraGo may also continue to acquire additional companies, assets or technologies principally related to, or complementary to, our current operations. Any such acquisitions will be accompanied by certain risks including but not limited to exposure to unknown liabilities of acquired companies, higher than anticipated acquisition costs and expenses, the difficulty and expense of integrating operations, systems, and personnel of acquired companies, disruption of the Company's ongoing business, inability to retain key customers, distributors, vendors and other business partners of the acquired company, diversion of management's time and attention; and possible dilution to shareholders.

Price Sensitive Market

The competitive market in which the Company conducts its business could require the Company to reduce its prices. If competitors offer discounts on certain products or services in an effort to recapture or gain market share or to sell other products, the Company may be required to lower prices or offer other favourable terms to compete successfully. Any such changes would likely reduce the Company's margins and could adversely affect operating results. Some of the Company's competitors may bundle services that compete with the Company for promotional purposes or as a long-term pricing strategy or provide guarantees of prices and product implementations. These practices could, over time, limit the prices that the Company can charge for its products. If the Company cannot offset price reductions with a corresponding increase in volume, bundling of services or with lower spending, then the reduced revenues resulting from lower prices would adversely affect the Company's margins and operating results.

Market Demand for Available Capacity

The Company currently has available capacity in its data centres and intends to expand its footprint in the cloud and data centre market. There can be no assurance that the existing or future market demand will be sufficient to fill this capacity. Should the demand for the Company's cloud and data centre services decline or fail to increase, this may negatively affect the Company's ability to capitalize on its high operating leverage and may adversely affect the Company's future financial performance.

Reductions in the amount or cancellations of customers' orders would adversely affect our business, results of operations and financial condition.

Cyber Security Risk

Our network security, data centre security and the authentication of our customer credentials are designed to protect unauthorized access to data on our network and to our data centre premises. Because techniques used to obtain unauthorized access to or to sabotage networks (including DDoS attacks) change frequently and may not be recognized until launched against a target, we may be unable to anticipate or implement adequate preventive measures against unauthorized access or sabotage. Consequently, unauthorized parties may overcome our network security and obtain access to confidential, customer or employee data on our network, including on a device connected to our network. In addition, because we own and operate our network, unauthorized access or sabotage of our network could result in damage to our network and to the computers or other devices used by our customer. An actual or perceived breach of network security or data centre security could harm public perception of the effectiveness of our security measures, adversely affect our ability to attract and retain customers, expose us to significant liability and adversely affect our business and revenue prospects.

The Company aims to mitigate and manage certain cyber security risks by employing specific policies and procedures, carrying out IT security-related audits, obtaining IT security-related compliance certificates, designating a security officer that oversees the IT security of the Company, designating a privacy officer that is accountable for the Company's compliance with applicable privacy laws, using DDoS mitigation, tools and services, utilizing back-up and disaster recovery services and maintaining specific cyber liability insurance coverage to insure against cyber security incidents.

Excessive Customer Churn

The successful implementation of our business strategy depends upon controlling customer churn. Customer churn is a measure of customers who stop using our services. Customer churn could increase as a result of:

- billing errors and/or reduction in the quality of our customer service;
- interruptions to the delivery of services to customers;
- the availability of competing technology and other emerging technologies, some of which may, from time to time, be less expensive or technologically superior to those offered by us; and

- competitive conditions in the industry, including strategic initiatives by us or our competitors, new services, service announcements and changes in pricing policy by us or our competitors.

An increase in customer churn can lead to slower customer growth, increased costs and a reduction in revenue. Given the current economic environment, there is risk that churn levels could increase in the future.

Insufficient Capital
The continued growth and operation of our business may require additional funding for working capital, debt service, the enhancement and upgrade of our network, the build-out of infrastructure to expand the coverage area of our services, possible acquisitions and possible bids to acquire spectrum licences. We may be unable to secure such funding when needed in adequate amounts or on acceptable terms, if at all.

To execute our business strategy, we may issue additional equity securities in public or private offerings, potentially at a price lower than the market price at the time of such issuance. Similarly, we may seek debt financing and we may be forced to incur significant interest expense. If we cannot secure sufficient funding, we may be forced to forego strategic opportunities or delay, scale back or eliminate network deployments, operations, acquisitions, spectrum acquisitions and other investments.

Reliance on Credit Facilities and Restrictive Debt Covenants
The Company relies on its Credit Facilities to operate its business, including for the maintenance of a certain level of liquidity and to carry out its strategy. There can be no assurance that the Company will continue to have access to appropriate Credit Facilities on reasonable terms and conditions, if at all beyond the maturity date of June 30, 2018 for the existing Credit Facilities. An inability to draw down upon the Credit Facilities could have a material adverse effect on the Company's business, liquidity, financial condition and results of operations.

Covenants in our Credit Facilities with our lenders impose operating and financial restrictions on us. A breach of any of these covenants could result in a default under our Credit Facilities. These restrictions may limit our ability to obtain additional financing, withstand downturns in our business and take advantage of business opportunities. Moreover, we may be required to seek additional debt financing on terms that include more restrictive covenants, may require repayment on an accelerated schedule or may impose other obligations that limit our ability to grow our business, acquire needed assets, or take other actions we might otherwise consider appropriate or desirable.

Key Competitors are More Established and Have More Resources
The market for internet access, data connectivity, cloud and data centre services is highly competitive and we compete with several other companies within each of our markets. Many of our competitors are better established or have greater financial resources than we have. Our competitors include:

- ILECs and CLECs providing DSL and fibre-optic enabled services over their existing wide, metropolitan and local area networks and who have started to provide cloud and colocation services;
- Utelcos offering or planning to offer internet and data connectivity over fibre optic networks;
- Large cloud service providers and IT companies;
- Colocation and disaster recovery service providers;
- cable operators offering high-speed Internet connectivity services and voice communications;
- wireless Internet service providers using licenced or licence-exempt spectrum;
- satellite and fixed wireless service providers offering or developing broadband Internet connectivity and VoIP; and
- resellers providing wireless Internet or other wireless services using infrastructure developed and operated by others.

Many of our competitors are well established with larger and better developed networks and support systems, longer standing relationships with customers and suppliers, greater name recognition and greater financial, technical and marketing resources than we have. Our competitors may subsidize competing services with revenue from other sources and, thus, may offer their products and services at prices lower than ours. We may not be able to reduce our prices which may make it more difficult to attract and retain customers.

We expect other existing and prospective competitors to adopt technologies and/or business plans similar to ours, or seek other means to develop services competitive with ours, particularly if our services prove to be attractive in our target markets.

Acquisitions and Other Strategic Transactions

We may from time to time make strategic acquisitions of other assets and businesses. Any such transactions can be risky, may require a disproportionate amount of our management and financial resources and may create unforeseen operating difficulties or expenditures, including:

- difficulties in integrating acquired businesses and assets into our business while maintaining uniform standards, controls, policies and procedures;
- obligations imposed on us by counterparties in such transactions that limit our ability to obtain additional financing, our ability to compete in geographic areas or specific lines of business or other aspects of our operational flexibility;
- increasing cost and complexity of assuring the implementation and maintenance of adequate internal control and disclosure controls and procedures;
- difficulties in consolidating and preparing our financial statements due to poor accounting records, weak financial controls and, in some cases, procedures at acquired entities not based on IFRS, particularly those entities in which we lack control; and
- inability to predict or anticipate market developments and capital commitments relating to the acquired company, business or assets.

If we do not successfully address these risks or any other problems encountered in connection with an acquisition, the acquisition could have a material adverse effect on our business, results of operations and financial condition. In addition, if we proceed with an acquisition, our available cash may be used to complete the transaction, diminishing our liquidity and capital resources, or additional equity may be issued which could cause significant dilution to existing shareholders.

Changes to Technologies and Standards

The industries TeraGo operates is characterized by rapidly changing technology, evolving industry standards and increasingly sophisticated customer requirements. The introduction of new or alternative technology and the emergence of new industry standards may render our existing network, equipment and/or infrastructure obsolete and our services unmarketable and may exert price pressures on existing services. It is critical to our success that we be able to anticipate changes in technology or in industry standards and ensure that we can leverage such new technologies and standards in a timely and cost-effective manner to remain competitive from a service and cost perspective.

Investments in Development of New Technologies, Products and Services

The Company has and will continue to make significant investments in the development and introduction of new products and services that make use of the Company's network, infrastructure and equipment. There is no assurance that the Company will be successful in implementing and marketing these new products and services in a reasonable time, or that they will gain market acceptance. Development could be delayed for reasons beyond our control. Alternatively, we may fail to anticipate or satisfy the demand for certain products or services, or may not be able to offer or market these new products or services successfully to customers. The failure to attract customers to new products or services, cross-sell service to our existing customer base or failure to keep pace with changing consumer preferences for products or services would slow revenue growth and could have a materially adverse effect on our business, results of operations and financial condition.

Expanding, Upgrading and Maintaining Network and Infrastructure

We expect to allocate significant resources in expanding, maintaining and improving our network. Additionally, as the number of our customer locations increases, as the usage habits of our customers change and as we increase our service offerings, we may need to upgrade our network to maintain or improve the quality of our services. If we do not successfully implement upgrades to our network, the quality of our services may decline and our churn rate may increase.

We may experience quality deficiencies, cost overruns and delays with the expansion, maintenance and upgrade of our network and existing infrastructure including the portions of those projects not within our control. Expansion of our network or infrastructure may require permits and approvals from governmental bodies and third parties. Failure to receive approvals in a timely fashion can delay expansion of our network. In addition, we are typically required to obtain rights from land, building and tower owners to install the antennas and other equipment that provide our internet access service to our customers. We may not be able to obtain, on terms acceptable to us or at all, the rights necessary to expand our network or existing infrastructure.

We also may face challenges in managing and operating our network and existing infrastructure. These challenges include ensuring the availability of customer equipment that is compatible with our network and managing sales, advertising, customer support, and billing and collection functions of our business while providing reliable network service that meets our customers' expectations. Our failure in any of these areas could adversely affect customer satisfaction, increase churn, increase our costs, decrease our revenue and otherwise have a material adverse effect on our business, prospects, financial condition and results of operations.

Reliance on Certain Third Parties
We rely on third-party suppliers, in some cases sole suppliers or limited groups of suppliers, to provide us with components necessary for the operation and upgrading of our network and infrastructure. If we are unable to obtain sufficient allocations of components, our network expansion will be delayed, we may lose customers and our profitability will be affected. Reliance on suppliers also reduces our control over costs, delivery schedules, reliability and quality of components. Any inability to obtain timely deliveries of quality components, or any other circumstances that would require us to seek alternative suppliers, could adversely affect our ability to expand and maintain our network or infrastructure.

In addition, the Company relies on third party partners, agents and resellers to carry out its business. If these third parties do not honour their contractual commitments or cease to do business, it may have a significant impact on our business. Replacements for such third parties may require a lengthy period of time in order to establish a commercially comparable relationship.

Foreign Exchange
While the majority of the Company's revenues are earned in Canadian dollars, a portion of its costs, including for certain capital expenditures are paid in U.S. dollars. As a result, the Company is exposed to currency exchange rate risks. A change in the currency exchange rate may increase or decrease the amount of Canadian dollars required to be paid by the Company for its U.S. expenditures. The Company does not currently have any foreign exchange contracts to manage the foreign exchange risk. As a result, there can be no assurance that currency fluctuations will not have a material adverse effect on the Company.

Interest Rates
As the Company currently borrows funds through its credit facility, certain portions of the facility are based on a variable interest rate. A significant rise in interest rates may materially increase the cost of either its revolving or non-revolving credit facilities. The Company mitigates a portion of the underlying interest rate risk with respect to the non-revolving term credit facility by entering into an interest rate swap contract to effectively fix the underlying interest rate on a variable rate debt. Similar interest rate swap contracts have not been entered into for the other portions of the credit facility. To the extent funds have been drawn down from such facilities, the Company will be exposed to interest rate fluctuations.

Regulatory Environment
We are subject to the laws of Canada and to regulations set by regulatory authorities of the Canadian government, primarily the CRTC and Industry Canada. Regulatory authorities may adopt new laws, policies or regulations, or change their interpretation of existing laws, policies or regulations, that could cause our existing authorizations to be changed or cancelled, require us to incur additional costs, or otherwise adversely affect our operations, revenue or cost of capital.

Any currently held regulatory approvals or licences may be subject to rescission and non-renewal. Additional approvals or licences may be necessary that we may not be able to obtain on a timely basis or on terms that are not unduly burdensome. Further, if we fail to obtain or maintain particular approvals on acceptable terms, such failure could delay or prevent us from continuing to offer some or all of our current or new services, or offer new services, and adversely affect our results of operations, business prospects and financial condition. Even if we were able to obtain the necessary approvals, the licences or other approvals we obtain may impose significant operational restrictions. The acquisition, lease, maintenance and use of spectrum are extensively regulated in Canada.

These regulations and their application are subject to continual change as new legislation, regulations or amendments to existing regulations are adopted from time to time by governmental or regulatory authorities, including as a result of judicial interpretations of such laws and regulations. Current regulations directly affect the breadth of services we are able to offer and may impact the rates, terms and conditions of our services.

The breach of the conditions of a licence or applicable law, even if inadvertent, can result in the revocation, suspension, cancellation or reduction in the term of a licence or the imposition of fines. In addition, regulatory authorities may grant new licences to third parties, resulting in greater competition in markets where we already have rights to licenced

spectrum. In order to promote competition, licences may also require that third parties be granted access to our bandwidth, frequency capacity, facilities or services. We may not be able to obtain or retain any required licence, and we may not be able to renew our licences on favourable terms, or at all.

Our internet access services may become subject to greater regulation in the future. If we become subject to proceedings before the CRTC or Industry Canada with respect to our compliance with the relevant legislation and regulations relating to restrictions on foreign ownership and control, we could be materially adversely affected, even if it were ultimately successful in such a proceeding. There can be no assurance that a future CRTC or Industry Canada determination or events beyond our control will not result in our ceasing to comply with the relevant legislation or regulations. If this occurs, our ability to operate as a Canadian carrier under the *Telecommunications Act* or to hold, renew or secure licences under the *Radio Communication Act* could be jeopardized and our business, operating results and financial condition could be materially adversely affected.

Obtaining and Maintaining Licenced Spectrum in Certain Markets

To offer our internet services using licenced spectrum in Canada, we depend on our ability to acquire and maintain sufficient rights to use spectrum through ownership or long-term leases in each of the markets in which we operate or intend to operate. Obtaining the necessary amount of licenced spectrum can be a long and difficult process that can be costly and require a disproportionate amount of our resources. We may not be able to acquire, lease or maintain the spectrum necessary to execute our business strategy. In addition, we may spend significant resources to acquire spectrum licences, even if the amount of spectrum actually acquired in certain markets is not adequate to deploy our network on a commercial basis in all such markets.

Using licenced spectrum, whether owned or leased, poses additional risks to us, including:

- inability to satisfy build-out or service deployment or research and development requirements upon which our spectrum licences or leases are, or may be, conditioned;
- adverse changes to regulations or licence conditions governing our spectrum rights;
- inability to use the spectrum we have acquired or leased due to interference from licenced or licence-exempt operators in our band or in adjacent bands;
- refusal by Industry Canada to recognize our acquisition or lease of spectrum licences from others or our investments in other licence holders;
- inability to offer new services or to expand existing services to take advantage of new capabilities of our network resulting from advancements in technology due to regulations governing our spectrum rights;
- inability to control leased spectrum due to contractual disputes with, or the bankruptcy or other reorganization of, the licence holders;
- failure of Industry Canada to renew our spectrum licences as they expire and our failure to obtain extensions or renewals of spectrum leases before they expire;
- imposition by Industry Canada of new or amended conditions of licence, or licence fees, upon the renewal of our spectrum licences or in other circumstances;
- potentially significant increases in spectrum prices, because of increased competition for the limited supply of licenced spectrum in Canada; and
- invalidation of our authorization to use all or a significant portion of our spectrum, resulting in, among other things, impairment charges related to assets recorded for such spectrum.

We expect Industry Canada to make additional spectrum available from time to time. Additionally, other companies hold spectrum rights that could be made available for lease or sale. The availability of additional spectrum in the marketplace could change the market value of spectrum rights generally and, as a result, may adversely affect the value of our spectrum assets.

We also use radio equipment under individual radio licences issued by Industry Canada, and subject to annual renewal. We may not be able to obtain the licences we require thereby jeopardizing our ability to reliably deliver our internet services. Industry Canada may decline to renew our licences, or may impose higher fees upon renewal, or impose other conditions that adversely affect us. Industry Canada may decide to reassign the spectrum in the bands we use to other purposes, and may require that we discontinue our use of radio equipment in such bands.

Licence-exempt Spectrum

We presently utilize licence-exempt spectrum in connection with a majority of our internet customers. Licence-exempt or "free" spectrum is available to multiple simultaneous users and may suffer bandwidth limitations, interference and slowdowns if the number of users exceeds traffic capacity. The availability of licence-exempt spectrum is not unlimited and others do not need to obtain permits or licences to utilize the same licence-exempt spectrum that we currently or may in the future utilize, threatening our ability to reliably deliver or expand our services. Moreover, the prevalence of licence-exempt spectrum creates low barriers to entry in our business, creating the potential for heightened competition.

Regulation of Internet

Regulation of the Internet and the content transmitted through that medium is a topic that receives considerable political discussion from time to time, from both a "pro-regulation" and an "anti-regulation" perspective, including discussions on whether all internet traffic should be delivered equally. It is unclear as to what impact decisions made on either side of this issue by various political and governing bodies could have on us and our business or on the ability of our customers to utilize our internet services.

Interruption or Failure of Information Technology and Communications Systems

We have experienced service interruptions in some markets in the past and may experience service interruptions or system failures in the future. Our services depend on the continuing operation of our cloud and data centre, information technology and communications systems. Any service interruption adversely affects our ability to operate our business and could result in an immediate loss of revenue. If we experience frequent or persistent system, power or network failures, our reputation and brand could be permanently harmed. We may make significant capital expenditures to increase the reliability and security of our systems, but these capital expenditures may not achieve the results we expect.

Our systems and data centres are vulnerable to damage or interruption from earthquakes, terrorist attacks, floods, fires, power loss, telecommunications failures, computer viruses, computer denial of service attacks or other attempts to harm our systems, and similar events. Some of our systems are not fully redundant and our disaster recovery planning may not be adequate. The occurrence of a natural disaster or unanticipated problems at our network centres or data centres could result in lengthy interruptions in our service and adversely affect our operating results. The Company could also be required to make significant expenditures if the Company's systems were damaged or destroyed, or pay damages if the delivery of the Company's services to its customers were delayed or stopped by any of these occurrences.

Retention and Motivation of Personnel

We depend on the services of key technical, sales, marketing and management personnel. The loss of any of these key persons could have a material adverse effect on our business, results of operations and financial condition. Our success is also highly dependent on our continuing ability to identify, hire, train, motivate and retain highly qualified technical, sales, marketing and management personnel.

Competition for such personnel can be intense and we cannot provide assurance that we will be able to attract or retain highly qualified technical, sales, marketing and management personnel in the future. Our inability to attract and retain the necessary technical, sales, marketing and management personnel may adversely affect our future growth and profitability. It may be necessary for us to increase the level of compensation paid to existing or new employees to a degree that our operating expenses could be materially increased.

If we cannot hire, train and retain motivated and well-qualified individuals, we may face difficulties in attracting, recruiting and retaining various sales and support personnel in the markets we serve, which may lead to difficulties in growing our subscriber base.

Leased Data Centre Facilities

The Company's data centres are located in leased premises and there can be no assurance that the Company will remain in compliance with the Company's leases, that the landlord will continue to support the operation of the Company's data centre and that the leases will not be terminated despite negotiation for long term lease periods and renewal provisions. Termination of a lease could have a material adverse effect on the Company's business, results of operations and financial condition.

Electrical Power and Outages

The Company's data centres are susceptible to regional variations in the cost of power, electrical power outages, planned or unplanned power outages and limitations on availability of adequate power resources. Power outages can harm, and in the past, have harmed the Company's customers and its business, including the loss of customers' data

and extended service interruptions. While the Company attempts to limit exposure to system downtime by using backup generators and power supplies, the Company cannot limit the Company's exposure entirely even with these protections in place. With respect to any increase in energy costs, the Company may not always be able to pass these increased costs on to the Company's customers which could have a material adverse effect on the Company's business, results of operations and financial condition.

Litigation Risk and Intellectual Property Claims
Competitors or other persons may independently develop, patent technologies or copyright software that are substantially equivalent or superior to those we currently use or plan to use or that are necessary to permit us to deploy and operate our network, data centres or provide cloud services. Some of these patents, copyrights or rights may grant very broad protection to the owners. We cannot determine with certainty whether any existing third party intellectual property or the issuance of any third party intellectual property would require us to alter technology or software we use, obtain licences or cease certain activities. Defending against infringement claims, even meritless ones, would be time consuming, distracting and costly.

If we are found to be infringing the proprietary rights of a third party, we could be enjoined from using such third party's rights, may be required to pay substantial royalties and damages, and may no longer be able to use the intellectual property subject to such rights on acceptable terms or at all. Failure to obtain licences to intellectual property held by third parties on reasonable terms, or at all, could delay or prevent us from providing services to customers and could cause us to expend significant resources to acquire technology which includes non-infringing intellectual property.

If we have to negotiate with third parties to establish licence arrangements, or to renew existing licences, it may not be successful and we may not be able to obtain or renew a licence on satisfactory terms or at all. If required licences cannot be obtained, or if existing licences are not renewed, litigation could result.

Operating Losses
Our accumulated deficit at December 31, 2016 was $63.1 million and have incurred a net loss in the last three fiscal years. We cannot anticipate with certainty what our earnings, if any, will be in any future period. However, we could incur further net losses as we continue to expand our network into new and existing markets and pursue our business strategy in providing cloud and data centre services. Accordingly, our results of operations may fluctuate significantly, which may adversely affect the value of an investment in our Common Shares. We may also invest significantly in our business before we expect cash flow from operations to be adequate to cover our anticipated expenses.

Economic and Geopolitical Risk
The market for our services depends on economic and geopolitical conditions affecting the broader market. Economic conditions globally are beyond our control. In addition, acts of terrorism and the outbreak of hostilities and armed conflicts between countries can create geopolitical uncertainties that may affect the global economy. Downturns in the economy or geopolitical uncertainties may cause customers to delay or cancel projects, reduce their overall capital or operating budgets or reduce or cancel orders for our services, which could have a material adverse effect on our business, results of operations and financial condition

UPCOMING ACCOUNTING PRONOUNCEMENTS NOT YET ADOPTED

Certain new standards, interpretations, amendments and improvements to existing standards have been issued by the IASB. The standards impacted that may be applicable to the Company are as follows:

(a) IFRS 15 Revenue from Contracts with Customers

On May 28, 2014, the IASB issued IFRS 15 which supersedes existing standards and interpretations including IAS 18, Revenue and IFRIC 13, Customer Loyalty Programmes. IFRS 15 introduces a single model for recognizing revenue from contracts with customers with the exception of certain contracts under other IFRSs. The standard requires revenue to be recognized in a manner that depicts the transfer of promised goods or services to a customer and at an amount that reflects the expected consideration receivable in exchange for transferring those goods or services. This is achieved by applying the following five steps:

1. Identify the contract with a customer;
2. Identify the performance obligations in the contract;
3. Determine the transaction price;

4. Allocate the transaction price to the performance obligations in the contract; and
5. Recognize revenue when (or as) the entity satisfies a performance obligation.

IFRS 15 also provides guidance relating to the treatment of contract acquisition and contract fulfillment costs.

The standard is currently effective for annual periods beginning on or after January 1, 2018. The Company is assessing the impact of this standard on the consolidated financial statements. The extent of the impact has not yet been determined.

(b) IFRS 9 Financial Instruments

On July 24, 2014, the IASB issued the final publication of the IFRS 9 standard, superseding the current IAS 39, Financial Instruments: recognition and measurement ("IAS 39") standard. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39.

The standard is effective for annual periods beginning on or after January 1, 2018 with early adoption permitted. The Company is assessing the impact of this standard on the consolidated financial statements. The extent of the impact has not yet been determined.

(c) IFRS 16 Leases

On January 13, 2016, the IASB issued the final publication of the IFRS 16 standard, which will supersede the current IAS 17, Leases standard. Under IFRS 16, a lease will exist when a customer controls the right to use an identified asset as demonstrated by the customer having exclusive use of the asset for a period of time. IFRS 16 introduces a single accounting model for lessees and all leases will require an asset and liability to be recognized on the statement of financial position at inception.

The accounting treatment for lessors will remain largely the same as under IAS 17. The standard is effective for annual periods beginning on or after January 1, 2019 with early adoption permitted, but only if the entity is also applying IFRS 15. The extent of the impact of the adoption of this standard has not yet been determined.

INTERNAL CONTROL OVER FINANCIAL REPORTING AND DISCLOSURE CONTROLS AND PROCEDURES

Our President and Chief Executive Officer and Chief Financial Officer designed or caused to be designed under their supervision, TeraGo's disclosure controls and procedures and internal control over financial reporting.

TeraGo's disclosure controls and procedures are designed to provide reasonable assurance that material information relating to TeraGo is made known to management by others, particularly during the period in which the interim filings are being prepared and that information required to be disclosed by TeraGo in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation. TeraGo's disclosure controls and procedures includes controls and procedures designed to ensure that information required to be disclosed by TeraGo in its annual filings, interim filings or other reports filed or submitted under securities legislation is accumulated and communicated to management, as appropriate to allow timely decisions regarding required disclosure.

TeraGo's internal control over financial reporting are designed to provide reasonable assurance regarding reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. TeraGo's internal control over financial reporting includes those policies and procedures that: (i) pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of TeraGo; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with GAAP, and that receipts and expenditures of TeraGo are being made only in accordance with authorizations of management and directors of TeraGo; and (iii) are designed to provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of TeraGo's assets that could have a material effect on TeraGo's financial statements.

The control framework used to design TeraGo's internal control over financial reporting is based on the Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO 2013).

Due to its inherent limitations, internal control over financial reporting may not prevent or detect all misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may change.

There were no changes in the Company's internal controls over financial reporting for the year ended December 31, 2016 that have materially affected or are reasonably likely to materially affect internal controls over financial reporting. Management has concluded that there are no material weaknesses relating to the design of TeraGo's internal controls over financial reporting as of December 31, 2016.

EXECUTIVE MANAGEMENT CHANGES

Effective September 30, 2016, Antonio (Tony) Ciciretto was appointed as President and CEO of the Company.

Effective September 30, 2016, Stewart Lyons (President and CEO) was no longer with the Company.

Effective October 13, 2016, Michael Stephens (Vice President, Marketing) was no longer with the Company.

Effective December 8 2016, Ryan Lausman (Chief Operating Officer) was no longer with the Company.

Effective February 1, 2017, Ron Perrotta joined the Company as Vice President, Marketing & Strategy. Mr. Perrotta previously provided consulting services to the Company on an interim basis.

DEFINITIONS – IFRS, ADDITIONAL GAAP AND NON-GAAP MEASURES

IFRS Measures

Cost of services
Cost of services consists of expenses related to delivering service to customers and servicing the operations of our networks. These expenses include costs for the lease of intercity facilities to connect our cities, internet transit and peering costs paid to other carriers, network real estate lease expense, spectrum lease expenses and lease and utility expenses for the data centres and salaries and related costs of staff directly associated with the cost of services.

Gross profit margin %
Gross profit margin % consists of gross profit margin divided by revenue where gross profit margin is revenue less cost of services.

Other operating expenses
Other operating expenses includes sales commission expense, advertising and marketing expenses, travel expenses, administrative expenses including insurance and professional fees, communication expenses, maintenance expenses and rent expenses for office facilities.

Foreign exchange gain (loss)
Foreign exchange gain (loss) relates to the translation of monetary assets and liabilities into Canadian dollars using the exchange rate in effect at that date. The resulting foreign exchange gains and losses are included in net income in the period.

Finance costs
Finance costs consist of interest charged on our short- and long-term debt, amortization of deferred financing costs including expenses associated with closing our long-term debt facility and accretion expense on the Company's decommissioning and restoration obligations. The deferred financing costs are amortized using the effective interest method over the term of the loan.

Finance income
Finance income consists of interest earned on our cash and cash equivalent and short-term investment balances.

Additional GAAP Measures

Earnings (loss) from operations
Earnings (loss) from operations exclude foreign exchange gain (loss), income taxes, finance costs and finance income. We include earnings (loss) from operations as an additional GAAP measure in our consolidated statement of earnings. We consider earnings (loss) from operations to be representative of the activities that would normally be regarded as operating for the Company. We believe this measure provides relevant information that can be used to assess the consolidated performance of the Company and therefore, provides meaningful information to investors.

Non-GAAP Measures

Adjusted EBITDA
The term "EBITDA" refers to earnings before deducting interest, taxes, depreciation and amortization. The Company believes that Adjusted EBITDA is useful additional information to management, the Board and investors as it provides an indication of the operational results generated by its business activities prior to taking into consideration how those activities are financed and taxed and also prior to taking into consideration asset depreciation and amortization and it excludes items that could affect the comparability of our operational results and could potentially alter the trends analysis in business performance. Excluding these items does not necessarily imply they are non-recurring, infrequent or unusual. Adjusted EBITDA is also used by some investors and analysts for the purpose of valuing a company. The Company calculates Adjusted EBITDA as earnings before deducting interest, taxes, depreciation and amortization, foreign exchange gain or loss, finance costs, finance income, gain or loss on disposal of network assets, property and equipment, stock-based compensation and restructuring, acquisition-related and integration costs. Investors are cautioned that Adjusted EBITDA should not be construed as an alternative to operating earnings or net earnings determined in accordance with IFRS as an indicator of our financial performance or as a measure of our liquidity and cash flows. Adjusted EBITDA does not take into account the impact of working capital changes, capital expenditures, debt principal reductions and other sources and uses of cash, which are disclosed in the consolidated statements of cash flows.

Adjusted EBITDA does not have any standardized meaning under GAAP. TeraGo's method of calculating Adjusted EBITDA may differ from other issuers and, accordingly, Adjusted EBITDA may not be comparable to similar measures presented by other issuers. See "Results of Operations – Adjusted EBITDA" for reconciliation of net loss to Adjusted EBITDA.

MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying consolidated financial statements of TeraGo Inc. and its subsidiaries and all the information in Management's Discussion and Analysis are the responsibility of management and have been approved by the Board of Directors.

The consolidated financial statements have been prepared by management in accordance with International Financial Reporting Standards. The consolidated financial statements include certain amounts that are based on the best estimates and judgments of management and in their opinion present fairly, in all material respects, TeraGo Inc.'s financial position, results of operations and cash flows. Management has prepared the financial information presented elsewhere in the Management's Discussion and Analysis and has ensured that it is consistent with the consolidated financial statements, or has provided reconciliations where inconsistencies exist.

Management of TeraGo Inc., in furtherance of the integrity of the consolidated financial statements, has developed and maintains a system of internal controls. Management believes the internal controls provide reasonable assurance that transactions are properly authorized and recorded, financial records are reliable and form a proper basis for the preparation of consolidated financial statements and that TeraGo Inc.'s material assets are properly accounted for and safeguarded. The internal control processes include management's communication to employees of policies that govern ethical business conduct.

The Board of Directors is responsible for overseeing management's responsibility for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements. The Board carries out this responsibility through its Audit Committee.

The Audit Committee meets periodically with management and the Company's independent auditors to review the Company's reported financial performance and to discuss audit, internal controls, accounting policies, and financial reporting matters; and to review Management's Discussion and Analysis, the consolidated financial statements and the external auditors' report. The Audit Committee reports its findings to the Board of Directors for consideration when approving the consolidated financial statements for issuance to the shareholders. The Audit Committee also considers, for review by the Board of Directors and approval by the shareholders, the engagement or re-appointment of the external auditors.

The consolidated financial statements have been audited by KPMG LLP, the external auditors, in accordance with Canadian generally accepted auditing standards on behalf of the shareholders. KPMG LLP has full and free access to the Audit Committee.

February 23, 2017

"Antonio Ciciretto"

President and Chief Executive Officer

"Joe Prodan"

Chief Financial Officer

KPMG LLP
Vaughan Metropolitan Centre
100 New Park Place, Suite 1400
Vaughan ON L4K 0J3
Canada
Tel 905-265-5900
Fax 905-265-6390

INDEPENDENT AUDITORS' REPORT

To the Shareholders of TeraGo Inc.

We have audited the accompanying consolidated financial statements of TeraGo Inc., which comprise the consolidated statements of financial position as at December 31, 2016 and 2015, the consolidated statements of comprehensive loss, changes in equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

KPMG LLP, is a Canadian limited liability partnership and a member firm of the KPMG network of independent
member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity.
KPMG Canada provides services to KPMG LLP.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of TeraGo Inc. as at December 31, 2016 and 2015, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

KPMG LLP

Chartered Professional Accountants, Licensed Public Accountants

February 23, 2017
Vaughan, Canada

TERAGO INC.
Consolidated Statements of Financial Position
(In thousands)

	Note		December 31 2016		December 31 2015
Assets					
Cash and cash equivalents	6(a)	$	13,034	$	13,066
Accounts receivable	6(b)		3,673		3,306
Prepaid expenses and other assets			3,150		3,351
Total current assets			19,857		19,723
Network assets, property and equipment	7		44,161		48,520
Intangible assets	8		19,400		21,824
Goodwill	8		19,419		19,063
Deferred income taxes	13		-		700
Restricted cash	9		-		172
Total non-current assets			82,980		90,279
Total Assets		$	102,837	$	110,002
Liabilities					
Accounts payable and accrued liabilities		$	11,027	$	9,128
Current portion of deferred revenue			287		211
Current portion of long-term debt	10		5,170		6,123
Current portion of other long-term liabilities	11		774		186
Total current liabilities			17,258		15,648
Decommissioning and restoration obligations	12		207		234
Deferred revenue			323		270
Long-term debt	10		35,608		39,658
Other long-term liabilities	11		793		1,977
Total non-current liabilities			36,931		42,139
Total Liabilities			54,189		57,787
Shareholders' Equity					
Share capital	14		86,171		85,636
Contributed surplus			25,620		25,408
Deficit			(63,143)		(58,829)
Total Shareholders' Equity		$	48,648	$	52,215
Total Liabilities and Shareholders' Equity		$	102,837	$	110,002
Commitments	19				

On behalf of the Board:

(signed) “Jim Nikopoulos”
Director

(signed) “Gary Sherlock”
Director

The accompanying notes are an integral part of these financial statements.

TERAGO INC.
Consolidated Statements of Comprehensive Loss
(In thousands, except per share amounts)

	Note		Year ended December 31 2016		Year ended December 31 2015
Revenue	17	$	59,086	$	57,720
Expenses					
Cost of services			13,477		13,159
Salaries and related costs			21,195		20,587
Other operating expenses			10,845		10,062
Depreciation of network assets, property and equipment	7		11,796		11,400
Amortization of intangible assets	8		3,529		3,697
			60,842		58,905
Loss from operations			(1,756)		(1,185)
Foreign exchange gain (loss)			16		(171)
Finance costs			(1,882)		(2,624)
Finance income			8		37
Loss before income taxes		$	(3,614)	$	(3,943)
Income taxes					
Income tax recovery (expense)	13		(700)		1,133
Net loss and comprehensive loss		$	(4,314)	$	(2,810)
Deficit, beginning of year		$	(58,829)	$	(56,019)
Deficit, end of year		$	(63,143)	$	(58,829)
Basic loss per share	16	$	(0.30)	$	(0.22)
Diluted loss per share	16	$	(0.30)	$	(0.22)
Basic weighted average number of shares outstanding			14,177		13,069
Diluted weighted average number of shares outstanding			14,177		13,069

The accompanying notes are an integral part of these financial statements.

TERAGO INC.
Consolidated Statements of Cash Flows
(In thousands)

	Note	Year ended December 31 2016	Year ended December 31 2015
Operating Activities			
Net loss for the year		$ (4,314)	$ (2,810)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:			
Severance, acquisition, and other costs		3,650	2,278
Depreciation of network assets, property and equipment	7	11,796	11,400
Amortization of intangible assets	8	3,529	3,697
Stock-based compensation expense	15	866	1,272
Finance costs		1,882	2,624
Finance income		(8)	(37)
Income tax expense (recovery)		700	(1,133)
Loss on adjustments and disposal of network assets	7	397	266
Severance, acquisition, and other costs paid		(1,943)	(2,153)
Changes in non-cash working capital items:			
Accounts receivable		(367)	1,001
Prepaid expenses		201	(689)
Accounts payable and accrued liabilities		(160)	480
Deferred revenue		129	(510)
Cash from Operating Activities		16,358	15,686
Investing Activities			
Acquisitions, net of cash acquired	5	(1,102)	(31,244)
Change in restricted cash		172	(172)
Purchase of network assets, property and equipment	7	(7,697)	(8,542)
Purchase of intangible assets	8	(496)	(892)
Change in non-cash working capital related to network assets, property and equipment and intangible assets		(442)	(239)
Cash used in Investing Activities		(9,565)	(41,089)
Financing Activities			
Proceeds from exercise of stock options		182	1,234
Proceeds from equity offering	14	-	10,004
Equity offering costs incurred	14	-	(794)
Interest paid, net of received		(1,746)	(1,904)
Proceeds from long term debt	10	-	31,500
Repayment of long-term debt	10	(5,261)	(4,058)
Financing costs incurred	10	-	(379)
Cash from (used in) Financing Activities		(6,825)	35,603
Net change in cash and cash equivalents, during the year		(32)	10,200
Cash and cash equivalents, beginning of year		13,066	2,866
Cash and cash equivalents, end of year		$ 13,034	$ 13,066
Supplemental cash flow disclosure			
Issuance of common shares in acquisition of RackForce Networks Inc.		$ -	$ 2,351

The accompanying notes are an integral part of these financial statements.

TERAGO INC.
Consolidated Statements of Changes in Equity
(In thousands)

	Share Capital				Contributed				
	Number		Amount		Surplus		Deficit		Total
Balance, January 1, 2016	14,133	$	85,636	$	25,408	$	(58,829)	$	52,215
Issuance of shares upon exercise of options	46		182		-		-		182
Stock-based compensation	-		-		212		-		212
Issuance of shares for directors' fees	71		353		-		-		353
Net loss and comprehensive loss	-		-		-		(4,314)		(4,314)
Balance, December 31, 2016	14,250	$	86,171	$	25,620	$	(63,143)	$	48,648

	Share Capital				Contributed				
	Number		Amount		Surplus		Deficit		Total
Balance, January 1, 2015	11,698	$	72,470	$	24,962	$	(56,019)	$	41,413
Issuance of shares upon exercise of options	287		1,234		-		-		1,234
Stock-based compensation	-		-		446		-		446
Issuance of shares for directors' fees	64		371		-		-		371
Issuance of shares for RackForce acquisition	329		2,351		-		-		2,351
Issuance of shares for equity offering – net of issuance costs	1,755		9,210		-		-		9,210
Net loss and comprehensive loss	-		-		-		(2,810)		(2,810)
Balance, December 31, 2015	14,133		85,636		25,408		(58,829)		52,215

See Note 14 – Share capital for classes of shares.

1. Reporting Entity

TeraGo Inc. (the "Company") provides businesses across Canada and globally with connectivity services, colocation services and enterprise infrastructure cloud services. The Company's head office is located in Canada at Suite 800 – 55 Commerce Valley Drive West, Thornhill, Ontario. The Company was incorporated under the Canada Business Corporations Act on December 21, 2000 and owns and operates a carrier-grade, fixed wireless, fibre-based, IP communications network, as well as cloud and colocation facilities in Canada targeting enterprise customers that require cloud, colocation, and connectivity services. The Company's common shares are listed on the Toronto Stock Exchange (TSX) under the symbol TGO.

2. Basis of Preparation and Presentation

(a) Basis of preparation

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB").

Certain comparative figures have been reclassified to conform with the financial statement presentation adopted for the current year.

The Board of Directors authorized the consolidated financial statements for issue on February 23, 2017.

(b) Basis of Measurement

The consolidated financial statements have been prepared on a historical cost basis except for the following material items in the statement of financial position:

- financial instruments at fair value through profit (loss) ("FVTPL") are measured at fair value through net income or loss

- liabilities for cash-settled stock-based payment arrangements are measured at fair value

(c) Functional and Presentation Currency

These consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency.

(d) Use of Estimates and Judgments

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Estimates and assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Key areas of estimation and information about critical judgments in applying accounting policies that have the most significant effect on amounts recognized in the consolidated financial statements are:

(i) Estimates of useful lives of network assets, property and equipment and intangible assets:
Management's judgment involves consideration of intended use, industry trends and other factors in determining the expected useful lives of depreciable assets, to determine depreciation methods, the asset's residual value and whether an asset is a qualifying asset for the purposes of capitalizing borrowing costs.

(ii) Capitalization of costs:
Judgments and estimates are used in assessing the direct labour and other costs capitalized to network assets, property and equipment.

(iii) Cash generating units:
Judgment is required to assess the Company's determination of cash generating units for the purpose of impairment testing.

(iv) Impairment of non-financial assets:

The process to calculate the recoverable amount of our cash generating unit requires use of valuation methods such as the discounted cash flow method which uses assumptions of key variables including future cash flows, discount rate and terminal growth rates.

(v) *Allowance for doubtful accounts:*
In developing the estimates for an allowance against existing receivables, the Company considers general and industry economic and market conditions as well as credit information available for the customer and the aging of the account. Changes in the carrying amount due to changes in economic and market conditions could significantly affect the loss for the period.

(vi) *Stock-based compensation:*
Estimating fair value for stock-based payments requires determining the most appropriate valuation model for a grant, which is dependent on the terms and conditions of the grant. In valuing stock options, the Company uses the Black-Scholes option pricing model. Several assumptions are used in the underlying calculation of fair values of the Company's stock options using the Black-Scholes option pricing model including the expected life of the option, risk-free interest rate and volatility of the underlying stock.

(vii) *Business combination:*
The amount of goodwill initially recognized as a result of a business combination, the fair value estimate of any contingent consideration and the determination of the fair value of the identifiable assets acquired and the liabilities assumed is based, to a considerable extent, on management's estimate of future cash flows expected to be derived from the assets acquired.

(viii) *Income taxes:*
A deferred tax asset is recognized for unused losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable income will be available against which they can be utilized. Significant estimates are required in evaluating the recoverability of deferred tax assets. The Company’s assessment is based on existing tax laws, estimates of future profitability and tax planning strategies.

(ix) *Provisions:*
Judgment is required to assess the likelihood of an outflow of the economic benefits to settle contingencies, such as litigations or decommissioning and restoration obligations, which may require a liability to be recognized. Significant judgments include assessing estimates of future cash flows, selection of discount rates and the probability of the occurrence of future events.

3. Significant Accounting Policies

(a) Revenue Recognition

The Company earns revenue by providing cloud, colocation, and connectivity services. Revenue is measured at the fair value of the consideration received or receivable for services, net of discounts and sales taxes. Revenue is recognized as the related services are provided to customers, if evidence of an arrangement exists, collection is deemed probable by management and revenue and costs are reliably measurable. The principal sources of revenue to the Company and recognition of these revenues are as follows:

(i) Monthly recurring revenue from cloud, colocation, and connectivity are recognized as service revenue ratably over the number of months in the contract term as related services are provided to the customer.
(ii) Revenue from installation services that do not have standalone value from the ongoing service are deferred and recognized over the term of the contract.
(iii) Usage revenue is recorded as service revenue in the month the usage occurs.

Billings or payments received from customers in advance of revenue recognition are recorded in deferred revenue on the consolidated statement of financial position.

(b) Basis of Consolidation

The consolidated financial statements include the accounts of TeraGo Inc., TeraGo Networks Inc. and its wholly owned subsidiaries RackForce Networks Inc., RackForce Cloud Video Inc, and Codeninja Ltd. (collectively, the Company). A subsidiary is an entity that is controlled by another entity, known as the parent. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. All intercompany transactions between subsidiaries are eliminated on consolidation. On January 1, 2017, subsequent to year-end,

TeraGo Networks Inc,, RackForce Networks Inc., RackForce Cloud Video Inc., and Codeninja Ltd were amalgamated.

(c) Financial Instruments

The Company initially measures financial instruments at fair value. Transaction costs that are directly attributable to the issuance of financial assets or liabilities are accounted for as part of the carrying value at inception (except for transaction costs related to financial instruments recorded as FVTPL financial assets which are expensed as incurred), and are recognized over the term of the assets or liabilities using the effective interest method.

Subsequent measurement and treatment of any gain or loss is recorded as follows:

(i) Financial assets and financial liabilities at FVTPL are measured at fair value at the balance sheet date with any gain or loss recognized immediately in net loss. Interest and dividends earned from financial assets are also included in net loss for the period.
(ii) Loans and receivables are measured at amortized cost using the effective interest method. Any gains or losses are recognized in net loss for the period.
(iii) Other financial liabilities are measured at amortized cost using the effective interest method. Any gains or losses are recognized in net loss for the period.

Impairment of Financial Assets

A financial asset carried at amortized cost is considered impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flow of that asset that can be estimated reliably. An impairment loss is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate.

In assessing impairment, the Company uses historical trends of the probability of default, timing of recoveries and the amount of loss incurred, adjusted for management's judgment as to whether current economic and credit conditions are such that the actual losses are likely to be greater or less than suggested by historical trends. Losses are recognized in the consolidated statements of loss and reflected in an allowance account against the financial asset.

The following is a summary of the Company's significant categories of financial instruments as at December 31, 2016:

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets currently are comprised of cash and cash equivalents, accounts receivable and restricted cash.

(i) ***Cash and Cash Equivalents and restricted cash***

Cash and cash equivalents consists of bank balances, cash on hand, demand deposits that can be withdrawn without penalty and short-term, highly liquid securities such as debt securities with an initial maturity date of not more than three months from the date of acquisition, that can readily be converted into known amounts of cash and are subject to an insignificant risk of change in value. Bank overdrafts that are repayable upon demand and form an integral part of the Company's cash management are included as a component of cash and cash equivalents. Cash and cash equivalents and restricted cash are carried at amortized cost.

(ii) ***Accounts Receivable***

Accounts receivable are measured at the amount the item is initially recognized. The allowance for doubtful accounts is based on the Company's assessment of the collectability of outstanding trade receivables. The evaluation of collectability of customer accounts is done on an individual account basis. If, based on an evaluation of accounts, it is concluded that it is probable that a customer will not be able to pay all amounts due, an expected impairment loss is recognized. Recoveries are only recorded when objective verifiable evidence supports the change in the original allowance. Changes in the carrying amount of the allowance account are recognized in the statement of comprehensive loss for the period.

Other financial liabilities

The Company recognizes debt securities issues and subordinated liabilities on the date that they originated. All other financial liabilities are recognized initially on the date that the Company becomes a party to the contractual provisions. The Company has the following non-derivative financial liabilities: current and long-term debt, accounts payable and accrued liabilities, and current portion and long-term portion of other long term liabilities.

Such liabilities are recognized initially at fair value less any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortized cost using the effective interest method.

Interest on loans and borrowings is expensed as incurred unless capitalized for qualifying assets in accordance with IAS 23, Borrowing Costs. Loans and borrowings are classified as a current liability unless the Company has an unconditional right to defer settlement for at least 12 months after the end of the year.

Derivative instruments
The Company uses an interest rate swap contract to manage the risk associated with the fluctuations of interest rates on its long-term debt. Management does not apply hedge accounting on the interest rate swap contract. As a result, the interest rate swap contract is marked to market each period, resulting in a gain or loss in net loss for the year.

(d) Network Assets, Property and Equipment
Network assets, property and equipment are recorded at cost less accumulated depreciation and impairment charges, if any. These costs include expenditures directly attributable to the acquisition of the asset. The cost of self-constructed network assets includes the cost of materials and direct labour and any other costs directly attributable to bringing the assets to a working condition for their intended purpose. This includes direct costs to design, acquire and build the asset and include directly attributable internally and externally generated engineering and construction costs and equipment on-hand. They also include the cost of dismantling and removing items and restoring the site on which they are located and specifically attributable borrowing costs on qualifying assets. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset only when it is probable that future economic benefits associated with the item will flow to the Company and the costs of the item can be reliably measured. All other expenditures are charged to operating expenses as incurred.

When major components of an item of network assets and property and equipment have different useful lives, they are accounted for as separate items. Depreciation of network assets and property and equipment is based on the estimated useful life of the assets as follows:

	Estimated useful life/ Asset depreciation method
Network assets	6 to 25 years straight line
Cloud and Data centre infrastructure	10 to 15 years straight line
Computer equipment	3 years straight line
Office furniture and equipment	5 years straight line
Leasehold improvements	over the term of lease
Vehicles	30% declining balance

Depreciation methods, useful lives and residual values are reviewed at least annually. Adjustments, if necessary, are recognized prospectively.

(e) Goodwill and Intangible Assets

Intangible assets include the following:

Radio Spectrum Licenses
Radio spectrum licenses are classified as indefinite life intangible assets and are not amortized but are tested for impairment on an annual basis. The licenses are granted with an auto-renewal policy and non-renewal of licenses by the regulatory body is considered remote unless license conditions are breached. As such, there is no foreseeable limit to the period over which these assets are expected to generate future net cash inflows to the Company and it is common industry practice for established telecommunications companies to treat these licenses as indefinite life.

Computer Software
Computer software is recorded at cost less accumulated amortization and amortized on a straight-line basis over 3 years or where there is a term license for the software, over the shorter of the term of the license or the useful life of the software.

Customer Relationships, Brand, Non-compete agreements, and Acquired Real Estate Leases
Customer relationships, brand, non-compete agreements and vendor's real estate leases are recorded at cost less accumulated amortization, initially measured at fair value on the acquisition date if acquired in a business combination. Customer relationships are amortized on a straight-line basis over a range of 5 to 10 years, brands are amortized over a period of 20 years, non-compete agreements are amortized on a straight-line basis in accordance with the term of the contracts and acquired real estate leases are amortized over the term of the lease.

Amortization methods, useful lives and residual values are reviewed at least annually. Adjustments, if necessary, are recognized prospectively.

Goodwill

Goodwill is the amount that results when the fair value of consideration transferred for an acquired business exceeds the net fair value of the identifiable assets and liabilities acquired. When the Company enters into a business combination, the acquisition method of accounting is used. Goodwill is assigned, as of the date of the business combination, to cash generating units that are expected to benefit from the business combination.

(f) Impairment of non-financial assets

The Company monitors events and changes in circumstances that may require an assessment of the recoverability of its non-financial long-lived assets. When an impairment test is performed, the recoverable amount is assessed by reference to the higher of i) the net present value of the expected future cash flows (value-in-use) and ii) the fair value less cost to sell. If the recoverable amount is estimated to be less than the carrying amount, the carrying amount of the asset is reduced to its recoverable amount and an impairment loss is charged to operations in the period in which the impairment is identified. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows ("cash generating units" or "CGUs").

The carrying values of identifiable intangible assets with indefinite lives and goodwill are tested at minimum annually for impairment. Goodwill and indefinite life intangible assets are allocated to CGUs for the purpose of impairment testing based on the level at which management monitors it, which is not higher than an operating segment. The allocation is made to those CGUs that are expected to benefit from the business combination in which the goodwill arose. The Company currently has assessed that it has a single CGU.

The carrying values of non-financial assets with finite useful lives, such as network assets, property and equipment and intangible and other assets subject to amortization, are assessed for impairment whenever events or changes in circumstances indicate that their carrying amounts may not be recoverable. If any such indication exists, the recoverable amount of the asset must be determined. Such assets are impaired if their recoverable amount is lower than their carrying amount. If it is not possible to estimate the recoverable amount of an individual asset, the recoverable amount of the CGU to which the asset belongs is tested for impairment.

(g) Subscriber acquisition costs

Subscriber acquisition costs are expensed as incurred.

(h) Business Combinations

Acquisitions of businesses are accounted for using the acquisition method. The consideration for each acquisition is measured at the aggregate of the fair values (at the date of exchange) of assets given, liabilities incurred or assumed, and equity instruments issued by the Company in exchange for control of the acquiree. Acquisition-related costs are recognized in loss in the period incurred.

Where applicable, the consideration for the acquisition includes any asset or liability resulting from a contingent consideration arrangement, measured at its acquisition-date fair value. Subsequent changes in such fair values are adjusted against the cost of acquisition where they qualify as measurement period adjustments. All other subsequent changes in the fair value of contingent consideration classified as an asset or liability are accounted for in accordance with relevant IFRS sections. Changes in the fair value of contingent consideration initially classified as equity are not recognized.

Where a business combination is achieved in stages, the Company's previously held interests in the acquired entity are remeasured to fair value at the acquisition date (i.e. the date the Company attains control) and the resulting gain or loss, if any, is recognized in profit or loss. Amounts arising from interests in the acquiree prior to the acquisition date that have previously been recognized in other comprehensive income are reclassified to profit or loss, where such treatment would be appropriate if that interest were disposed.

The acquiree's identifiable assets, liabilities and contingent liabilities that meet the conditions for recognition under IFRS 3 are recognized at their fair value at the acquisition date.

If the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the Company reports provisional amounts for the items for which the accounting is incomplete. Those provisional amounts are adjusted during the measurement period or additional assets or liabilities are

recognized, to reflect new information obtained about facts and circumstances that existed as of the acquisition date that, if known, would have affected the amounts recognized as of that date.

The measurement period is the period from the date of acquisition to the date the Company obtains complete information about facts and circumstances that existed as of the acquisition date and is subject to a maximum period of one year.

(i) Leases

Leases entered into by the Company as lessee that transfer substantially all the benefits and risks of ownership to the Company are recorded as finance leases and are included in property and equipment and obligations under finance leases. Obligations under finance leases are reduced by lease payments net of imputed interest. All other leases are classified as operating leases under which lease payments are expensed on a straight-line basis over the term of the lease. Lease incentives received are recognized as an integral part of the total lease cost, over the term of the lease. Contingent lease payments are accounted for in the period incurred.

(j) Provisions

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Where the impact is significant, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects the current market assessments of the time value of money and the risk specific to the liability. The unwinding of the discount is recognized as a finance cost.

Decommissioning and Restoration Obligations:

In the course of the Company's operations, network and other assets are utilized on leased premises. Often costs are expected to be incurred associated with decommissioning these assets and restoring the location where these assets are situated upon ceasing their use on those premises.

These decommissioning and restoration provisions are calculated on the basis of the identified costs for the current financial year, extrapolated into the future based on management's best estimates of future trends in prices, inflation, and other factors, and are discounted to present value at a risk-adjusted rate specifically applicable to the liability. Assumptions related to the amount and timing of cash flows required to satisfy the Company's future legal obligations include labour costs based on current marketplace wages and the rate of inflation over expected years to settlement; the length of facility lease renewal periods and probability of such renewals; and the appropriate discount rate to present value the future cash flows. Forecasts of estimated future provisions are reviewed periodically in light of future changes in business conditions or technological requirements.

The Company records these decommissioning and restoration costs as Network Assets, Property and Equipment, and subsequently allocates them to expense using a systematic and rational method over the asset's useful life. The Company records the accretion of the liability (unwinding of the discount) as a charge to finance costs.

(k) Foreign Currency Translation

Foreign currency accounts are translated into Canadian dollars as follows: At the transaction date, each asset, liability, revenue, and expense is translated into Canadian dollars using the exchange rate in effect at that date. At the year-end date, monetary assets and liabilities are translated into Canadian dollars by using the exchange rate in effect at that date. The resulting foreign exchange gains and losses are included in net loss in the current year.

(l) Finance income and finance costs

Finance income comprises interest income on funds invested, dividend income, gains on sale of available-for-sale financial assets, and changes in fair value of financial assets at FVTPL.

Finance costs comprise interest expense on borrowings, accretion of discounts on provisions, and changes in fair value of financial assets at FVTPL. Borrowing costs that are not directly attributable are recognized in loss for the year.

(m) Income Taxes

Income taxes on losses include current and deferred taxes. Income taxes are recognized in loss except to the extent that it relates to business combinations, or items recognized directly in equity or in other comprehensive income. Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is generally recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax assets and liabilities are measured, on an undiscounted basis, at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

Deferred tax assets and liabilities are recognized where the carrying amount of an asset or liability in the consolidated statement of financial position differs from its tax base, except for differences arising on:

- the initial recognition of goodwill;
- the initial recognition of an asset or liability in a transaction which is not a business combination and at the time of the transaction affects neither accounting or taxable profit; and
- investments in subsidiaries, branches and associates, and interests in joint ventures where the Company is able to control the timing of the reversal of the difference and it is probable that the difference will not reverse in the foreseeable future.

A deferred tax asset is recognized to the extent it is probable that it will be realized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent it is no longer probable the related tax benefit will be realized.

(n) Government incentives

From time to time, the Company applies for government incentive programs such as investment tax credits. Government incentives are recognized when there is reasonable assurance of realization and reflected as a reduction of the expenditure to which the incentive relates. In the event the investment tax credits received differs from the amount claimed, the difference will be reflected in operations in the year in which it is determined.

(o) Stock-based Compensation Plans

The Company has equity-settled and cash-settled stock-based compensation plans.

The grant date fair values of equity settled stock-based payment awards to employees and directors are recognized as compensation cost, with a corresponding increase to equity, over the vesting period of the award. For cash-settled awards, the awards are classified as a liability and are re-measured to fair value at each reporting date. The Company accounts for the effects of service and non-market performance conditions in measuring the fair value of the liability in cash-settled awards by adjusting the number of rights to receive cash that are expected to satisfy any service and non-market performance conditions on a best estimate basis.

Awards with graded vesting are valued and recognized as compensation cost based on the respective vesting tranche. The amount of compensation cost recognized is adjusted to reflect the number of awards expected to vest based on continued employment vesting conditions, such that the amount ultimately recognized as compensation cost is based on the number of awards that vest.

The Employee share purchase plan allows employees to voluntarily participate in a share purchase plan. Under the terms of the plan, employees can contribute a specified percentage of their regular earnings through payroll deductions and the Company makes a contribution match which is recorded as compensation expense.

(p) Operating Segments

Management has determined that the Company operates in a single reportable operating segment. The Company provides cloud, colocation, and connectivity services and earns revenues primarily in Canada. As at December 31, 2016 substantially all of the Company's identifiable assets are located in Canada, with an immaterial amount of assets located in the United States and the United Kingdom.

(q) Loss Per Share

The basic loss per share has been computed by dividing the net loss for the year by the weighted average number of common shares outstanding during the year. Diluted loss per share is computed by adjusting the net loss attributable to common shareholders for the year and the weighted average number of common shares outstanding for the period for the effects of all potentially dilutive common shares including shares subject to the exercise of stock options, where dilutive. The Company uses the treasury stock method for calculating diluted loss per share.

4. Upcoming accounting pronouncements not yet adopted

The IASB has issued new standards and amendments to existing standards. These changes are not yet adopted as at December 31, 2016 and could have an impact on future periods.

IFRS 15 Revenue from Contracts with Customers

On May 28 2014, the IASB issued IFRS 15 which supersedes existing standards and interpretations including IAS 18, Revenue and IFRIC 13, Customer Loyalty Programmes. IFRS 15 introduces a single model for recognizing revenue from contracts with customers with the exception of certain contracts under other IFRSs. The standard requires revenue to be recognized in a manner that depicts the transfer of promised goods or services to a customer and at an amount that reflects the expected consideration receivable in exchange for transferring those goods or services. This is achieved by applying the following five steps:

1. Identify the contract with a customer;
2. Identify the performance obligations in the contract;
3. Determine the transaction price;
4. Allocate the transaction price to the performance obligations in the contract; and
5. Recognize revenue when (or as) the entity satisfies a performance obligation.

IFRS 15 also provides guidance relating to the treatment of contract acquisition and contract fulfillment costs.

The standard is effective for annual periods beginning on or after January 1, 2018. The Company is assessing the impact of this standard on the consolidated financial statements. The extent of the impact of IFRS 15 has not yet been determined.

IFRS 9 Financial Instruments

On 24 July 2014, the IASB issued the final publication of the IFRS 9 standard, superseding the current IAS 39, Financial Instruments: recognition and measurement ("IAS 39") standard. IFRS 9 includes revised guidance on the classification and measurement of financial instruments, including a new expected credit loss model for calculating impairment on financial assets, and the new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39.

The standard is effective for annual periods beginning on or after January 1, 2018 with early adoption permitted. The Company is assessing the impact of this standard on the consolidated financial statements. The extent of the impact has not yet been determined.

IFRS 16 Leases

On January 13, 2016, the IASB issued the final publication of the IFRS 16 standard, which will supersede the current IAS
17, Leases standard. Under IFRS 16, a lease will exist when a customer controls the right to use an identified asset as demonstrated by the customer having exclusive use of the asset for a period of time. IFRS 16 introduces a single accounting model for lessees and all leases will require an asset and liability to be recognized on the statement of financial position at inception.

The accounting treatment for lessors will remain largely the same as under IAS 17. The standard is effective for annual periods beginning on or after January 1, 2019 with early adoption permitted, but only if the entity is also applying IFRS 15. The extent of the impact of the adoption of this standard has not yet been determined.

5. Business Combinations

AirVM Hosting Business

On May 26, 2016, the Company closed an asset purchase agreement to acquire the Hosting Business of Ottawa-based AirVM Inc for consideration of $1,102. The acquisition brings expanded Infrastructure as a Service (Iaas) offerings to the Company from locations in the United States and the United Kingdom.

The acquisition was accounted for using the acquisition method in accordance with IFRS 3, Business Combinations, with the results of operations consolidated with those of the Company effective from the acquisition date. In connection with the acquisition, the Company recorded network assets, property and equipment of $137, customer relationships and other intangible assets of $609, and goodwill of $356.

Goodwill recognized in the transaction represents the expected operational synergies with the acquiree including intangible assets that do not qualify for separate recognition. The goodwill and intangibles assets are tax deductible.

The identifiable intangible assets are being amortized over a period of 2 to 5 years.

Acquisition of RackForce Networks Inc.

On March 27, 2015, the Company closed a share purchase agreement to acquire 100% of the shares of RackForce Networks Inc. ("RackForce"). The acquisition supports TeraGo's strategic plan to offer complementary services to business and enterprise customers. RackForce is one of Canada's largest enterprise cloud service providers. Its business involves the management of enterprise cloud services including Cloud Hosting Services (IaaS) and Application Hosting Services (SaaS) with network. RackForce has been in operation since 2001 and currently serves a variety of enterprise customers, including Fortune 100 companies, governments and education clients.

On March 27, 2015, the Company transferred $33,351 (consisting of $31,000 cash and issuance of $2,351 common shares of the Company) with payment of cash and shares of $24,132 to the vendors and cash of $9,219 paid in escrow for the remaining balance, subject to among other things a working capital adjustment to be finalized within 90 days of closing. During 2015 the Company rendered a reduction in the purchase consideration of $666 from the working capital adjustment, resulting in a net purchase consideration of $32,685. The Company was repaid $666 from the escrow account in 2015.

The acquisition was accounted for using the acquisition method in accordance with IFRS 3, Business Combinations, with the results of operations consolidated with those of the Company effective the acquisition date. Total acquisition related costs were $656 and were included in other operating expenses for the year ended December 31, 2015.

The fair values of the assets acquired and liabilities assumed at the date of acquisition were as follows:

Net Working Capital	$	(621)
Network Assets, Property and Equipment		9,824
Identifiable Intangible Assets:		
Customer Relationships		11,170
Brand		2,460
Non-Competition Agreements		490
Deferred tax liability		(3,039)
Goodwill		12,401
Purchase Price	$	32,685

Goodwill represents the expected operational synergies with the acquiree including intangible assets that do not qualify for separate recognition. The goodwill is not tax deductible.

The customer relationships are being amortized over a period of 10 years, brand is being amortized over a period of 20 years and the non-competition agreements are being amortized over a period of 3 years.

Acquisition of BoxFabric

On September 18, 2015, the Company closed a share purchase agreement to acquire 100% of the shares of Codeninja Ltd., which operates as BoxFabric ("BoxFabric") for consideration of $1,100, subject to a working capital adjustment.

The acquisition was accounted for using the acquisition method in accordance with IFRS 3, Business Combinations, with the results of operations consolidated with those of the Company effective from the acquisition date.

Following settlement of the working capital adjustment, the Company paid total consideration of $1,082, of which $172 was held in escrow as restricted cash pending finalization of the escrow term at December 31, 2015.

The fair values of the assets acquired and liabilities assumed at the date of acquisition are determined to be as follows:

Net working capital	$	20
Network Assets, Property and Equipment		46
Identifiable Intangible Assets		356
Deferred tax liability		(94)

Goodwill	754
Purchase Price	$ 1,082

Goodwill represents the expected operational synergies with the acquiree including intangible assets that do not qualify for separate recognition. The goodwill is not tax deductible.

The identifiable intangible assets are being amortized over a period of 3 to 5 years.

Pro Forma Disclosure

The Company's acquisition of the Hosting Business of AirVM Inc. contributed revenue of $395 and earnings from operations of $19 since the date of acquisition. If the acquisition had occurred on January 1, 2016, consolidated revenue of the Company for the year ended December 31, 2016 would have been $59,348 and loss from operations for the year would have been ($1,743).

6. Current Assets

Details of selected current asset balances are as follows:

(a) Cash and cash equivalents

The Company's cash and cash equivalents are comprised of bank balances at major Canadian financial institutions.

(b) Accounts receivable

The Company's accounts receivable are comprised of the following:

	December 31 2016	December 31 2015
Trade receivables	$ 3,531	$ 3,148
Allowance for doubtful accounts	(124)	(54)
Other	266	212
	$ 3,673	$ 3,306

7. Network Assets, Property and Equipment

Cost	Network assets	Cloud & Datacentre infrastructure	Computer equipment	Office furniture and equipment	Leasehold improvements	Vehicles	Total
Balance, January 1, 2016	$ 114,869	$ 13,752	$ 2,173	$ 2,211	$ 1,602	$ 49	$ 134,656
Additions / reclassifications	6,530	645	355	121	46	-	7,697
Acquisitions	5	$ -	$ 132	$ -	$ -	$ -	$ 137
Disposals / Adjustments	(2,795)	(11)	-	-	-	-	(2,806)
Balance, December 31, 2016	**$ 118,609**	**$ 14,386**	**$ 2,660**	**$ 2,332**	**$ 1,648**	**$ 49**	**$ 139,684**
Accumulated Depreciation							
Balance, January 1, 2016	$ 80,080	$ 888	$ 2,133	$ 2,132	$ 854	$ 49	$ 86,136
Depreciation for the year	9,857	1,590	112	40	197	-	11,796
Disposals / Adjustments	(2,410)	1	-	-	-	-	(2,409)
Balance, December 31, 2016	**$ 87,527**	**$ 2,479**	**$ 2,245**	**$ 2,172**	**$ 1,051**	**$ 49**	**$ 95,523**
Net Book Value, December 31, 2016	**$ 31,082**	**$ 11,907**	**$ 415**	**$ 160**	**$ 597**	**$ -**	**$ 44,161**

Cost	Network assets	Cloud & Datacentre infrastructure	Computer equipment	Office furniture and equipment	Leasehold improvements	Vehicles	Total
Balance, January 1, 2015	$ 110,485	$ 1,663	$ 2,105	$ 2,194	$ 1,460	$ 49	$ 117,956
Additions / reclassifications	6,096	2,315	20	5	106	-	8,542
Acquisitions	-	$ 9,774	$ 48	$ 12	$ 36	$ -	$ 9,870
Disposals / Adjustments	(1,712)	-	-	-	-	-	(1,712)
Balance, December 31, 2015	**$** 114,869	**$** 13,752	**$** 2,173	**$** 2,211	**$** 1,602	**$** 49	**$** 134,656
Accumulated Depreciation							
Balance, January 1, 2015	$ 71,233	$ 195	$ 1,950	$ 2,094	$ 662	$ 48	$ 76,182
Depreciation for the year	10,294	692	183	38	192	1	11,400
Disposals / Adjustments	(1,447)	1	-	-	-	-	(1,446)
Balance, December 31, 2015	**$** 80,080	**$** 888	**$** 2,133	**$** 2,132	**$** 854	**$** 49	**$** 86,136
Net Book Value, December 31, 2015	**$** 34,789	**$** 12,864	**$** 40	**$** 79	**$** 748	**$** -	**$** 48,520

For the years ended December 31, 2016 and 2015, the Company had additions of capitalized wages and other directly attributable costs of $2,097 and $1,851, respectively, in network assets.

During 2016, the Company wrote off assets with a net book value of $397 (Cost of $2,806 less accumulated depreciation of $2,409). During 2015, the Company wrote off assets with a net book value of $266 (Cost of $1,712 less accumulated depreciation of $1,446). The corresponding loss on disposal of assets was included in other operating expenses.

8. Intangible Assets and Goodwill

Cost	Radio spectrum licenses	Computer Software	Customer relationships	Other	Total Intangibles	Goodwill	Total Intangibles and Goodwill
Balance, January 1, 2016	$ 7,041	$ 8,560	$ 17,677	$ 4,835	$ 38,113	$ 19,063	$ 57,176
Additions	-	496	-	-	496	-	496
Acquisitions	-	-	564	45	609	356	965
Balance, December 31, 2016	**$** 7,041	**$** 9,056	**$** 18,241	**$** 4,880	**$** 39,218	**$** 19,419	**$** 58,637
Accumulated Depreciation							
Balance, January 1, 2016	$ 2,371	$ 7,178	$ 5,385	$ 1,355	$ 16,289	$ -	$ 16,289
Amortization for the year	-	821	2,096	612	3,529	-	3,529
Balance December 31, 2016	**$** 2,371	**$** 7,999	**$** 7,481	**$** 1,967	**$** 19,818	**$** -	**$** 19,818
Net Book Value, December 31, 2016	**$** 4,670	**$** 1,057	**$** 10,760	**$** 2,913	**$** 19,400	**$** 19,419	**$** 38,819

Cost	Radio spectrum licenses	Computer Software	Customer relationships	Other	Total Intangibles	Goodwill	Total Intangibles and Goodwill
Balance, January 1, 2015	$ 7,041	$ 7,668	$ 6,180	$ 1,856	$ 22,745	$ 5,908	$ 28,653
Additions	-	892	-	-	892	-	892
Acquisitions	-	-	11,497	2,979	14,476	13,155	27,631
Balance, December 31, 2015	**$** 7,041	**$** 8,560	**$** 17,677	**$** 4,835	**$** 38,113	**$** 19,063	**$** 57,176
Accumulated Depreciation							
Balance, January 1, 2015	$ 2,371	$ 6,157	$ 3,293	$ 771	$ 12,592	$ -	$ 12,592
Amortization for the year	-	1,021	2,092	584	3,697	-	3,697
Balance December 31, 2015	**$** 2,371	**$** 7,178	**$** 5,385	**$** 1,355	**$** 16,289	**$** -	**$** 16,289
Net Book Value, December 31, 2015	**$** 4,670	**$** 1,382	**$** 12,292	**$** 3,480	**$** 21,824	**$** 19,063	**$** 40,887

Impairment

The annual impairment test of goodwill and indefinite life intangible assets was performed on December 31, 2016 and December 31, 2015 and did not result in any impairment loss.

The recoverable amount is the higher of (i) an asset's or CGU's fair value less costs to sell and (ii) its value-in-use. In performing the annual impairment test for the Company's single CGU, the Company measured the value-in-use of the CGU using certain key management assumptions. Cash flow projections, which were made over a five-year period, were based primarily on the financial budget reviewed by the Board of Directors plus a terminal value using a 3% terminal growth rate. The Company discounted these estimates of future cash flows to their present value using an after-tax discount rate of 10.5% which reflects the entity's weighted average cost of capital. The fair value less costs to sell, primarily based on the Company's market capitalization as at December 31, 2016, also significantly exceeded the net carrying amount of the CGU.

9. Restricted Cash

Funds Held in escrow

During the year, the $172 held back in escrow related to the acquisition of BoxFabric in 2015 (Note 5), was released by the Company pursuant to the terms of the share purchase agreement.

10. Long-term Debt

	December 31 2016	December 31 2015
Term debt facility (a)	$ 40,897	$ 45,833
Equipment loans (b)	170	431
less: financing fees	(289)	(483)
	40,778	45,781
less: current portion	(5,170)	(6,123)
	$ 35,608	$ 39,658

(a) Term Debt Facility

In June 2014, the Company entered into an agreement with a syndicate led by the National Bank of Canada ("NBC") to provide a $50,000 credit facility that is principally secured by a general security agreement over the Company's assets.

In March 2015, the Company entered into an amended agreement with the syndicate led by NBC that increased the credit facility by $35,000 ($30,000 increase to the term debt facility and $5,000 increase to the revolving facility) and extended the term from June 6, 2017 to June 30, 2018. Other terms were substantially consistent with the existing credit facilities.

The total $85,000 facility that matures June 30, 2018 is made up of the following:

- $10,000 revolving facility which bears interest at prime plus a margin percent. As of December 31, 2016, $nil amount is outstanding (December 31, 2015 - $nil). Letters of credit outstanding under the facility totaled $655 as of December 31, 2016 (December 31, 2015 - $655).

- $50,000 term facility which bears interest at prime or Banker's Acceptance (at the Company's option) plus a margin percent and is repayable in quarterly principal installments of $1,250. This facility was fully drawn upon signing the amended agreement.

  On December 31, 2016, $41,100 of the term facility principal balance outstanding was in a Banker's Acceptance and the remaining $150 was at a floating rate. In 2015, the Company entered into amended interest rate swap contracts that matures June 29, 2018. The interest rate on the Banker's Acceptance at December 31, 2016 was 3.99%. The interest rate swap contract has not been designated as a hedge and will be marked-to-market each quarter. The fair value of the interest rate swap contract at December 31, 2016 was a liability of $261 (December 31, 2015 – $612) and is recorded in other long-term liabilities (Note 11), with a corresponding charge for the change in fair value recorded in finance costs.

As at December 31, 2016, the Company prepaid interest in the amount of $353 which represents the net settlement of the Banker's Acceptance and is recorded as a reduction in the carrying value of the debt.

- $25,000 available for funding acquisitions and will bear interest at prime plus a margin percent and is repayable in quarterly principal installments of 2.5% of the aggregate amount outstanding. As of December 31, 2016, this facility remains undrawn.

The financing fees have been deferred and amortized using the effective interest method over the term of the facility.

The NBC facility is subject to certain financial and non-financial covenants which the Company is in compliance with at December 31, 2016. Under this facility, the Company is subject to a cash flow sweep that could accelerate a certain amount of principal repayment based on a calculation outlined by the credit agreement not later than 120 days after the end of each fiscal year.

(b) Equipment loans

The Company has certain equipment loans with financing companies that are secured by the underlying equipment. These debt facilities, which bear interest at fixed rates ranging from 5.97% to 6.23% over the respective terms, have maturity dates between September 2017 and December 2017 and have total monthly installments of $16.

11. Other Long-Term Liabilities

	December 31 2016	December 31 2015
Performance based share units (Note 15 (c))	$ 318	$ 309
Restricted share units (Note 15 (b))	707	441
Fair value of interest rate swap contract (Note 10 (a))	261	612
Lease inducement liability	281	331
Assumed liabilities - Vancouver Data Centre	-	470
	1,567	2,163
less: current portion	(774)	(186)
	$ 793	$ 1,977

12. Decommissioning and Restoration Obligations

The Company's hub sites are established in leased or licensed premises. As part of these arrangements, the Company is liable for all restoration costs to ensure that the space is returned to its original state upon termination of the leases. The decommissioning and restoration obligations related to future site restoration costs related to these arrangements or licenses. The decommissioning and restoration obligations were determined using a discount rate of 10.5% over a range of periods from 2025 to 2045. As at December 31, 2016, the estimated amount of undiscounted cash flows required to settle this liability was $1,163.

The following table presents the reconciliation of the beginning and ending aggregate carrying amount of the decommissioning and restoration obligations associated with the retirement of network assets:

	December 31 2016	December 31 2015
Obligation, beginning of year	$ 234	$ 222
Accretion expense included in finance costs	17	12
Changes in assumptions	(44)	-
Obligation, end of year	$ 207	$ 234

13. Income Taxes

Income tax expense (recovery)

	December 31 2016	December 31 2015
Current tax expense		
Current tax expense	$ -	$ -
	-	-
Deferred income tax (recovery)		
Movement in tax deductible temporary differences	700	(1,133)
	$ 700	$ (1,133)

Reconciliation of effective tax rate	December 31 2016	2016 %	December 31 2015	2015 %
Loss before Income taxes	$ (3,614)		$ (3,943)	
Income tax recovery at statutory rates	$ (958)	(26.5)	$ (1,031)	(26.1)
Permanent differences	150	4.2	410	10.4
Unrecognized (recognized) deferred tax assets	2,048	56.7	(512)	(13.0)
Other	(540)	(14.9)	-	-
Income tax expense (recovery)	$ 700	19.4	$ (1,133)	(28.7)

Unrecognized deferred tax assets and liabilities

Deferred tax assets have not been recognized in respect of the following items because they do not meet the criteria for recognition.

	December 31 2016	December 31 2015
Excess of tax basis over book value	$ 9,027	$ 9,410
Non-capital tax loss carryforwards	1,964	-
Other deductible temporary differences	1,478	1,011
	$ 12,469	$ 10,421

Movement in deferred tax balances

	Net Balance December 31, 2015	Recognized in net loss	Net Balance, December 31, 2016
Excess UCC over NBV	$ 2,021	$ (2,021)	$ -
SR&ED	872	(872)	-
Intangible Assets	(3,504)	3,504	-
Non-capital loss carryforwards	1,352	(1,352)	-
Other deductible temporary differences	(41)	41	-
	$ 700	$ (700)	$ -

In 2016, the Company determined based on objective negative evidence in the form of cumulative net losses, that it was more likely than not that the Company would not have taxable profits with which to utilize recognized deferred income tax assets in the near term. As a result, the Company recorded a reduction of the deferred income tax asset of $700 for the year ended December 31, 2016 with a corresponding charge to income tax expense.

Non-capital tax losses

The non-capital tax losses carried forward are available to reduce future taxable income and expire as follows:

2030	$	1,386
2031		1,356
2032		-
2033		718
2034		883
2035		1,695
2036		1,476
	$	7,514

14. Share Capital

Authorized

Unlimited Common Shares
Two Class B Shares, non-transferable unless approved by the Board, non-participating and redeemable. Holder of Class B shares are entitled to nominate and elect one director for each Class B Share held.

		In $		
Issued	**Number of Common Shares**	**Common Shares**	**Share Issue Costs**	**Total**
Balance, January 1, 2015	11,698	78,126	(5,656)	72,470
Issuance of common shares on exercise of stock options	287	1,234	-	1,234
Issuance of common shares for directors' fees	64	371	-	371
Issuance of common shares for Rackforce acquisition	329	2,351	-	2,351
Issuance of common shares for equity offering	1,755	10,004	(794)	9,210
Balance, December 31, 2015	14,133	92,086	(6,450)	85,636
Issuance of common shares on exercise of stock options	46	182	-	182
Issuance of common shares for directors' fees	71	353	-	353
Balance, December 31, 2016	14,250	92,621	(6,450)	86,171

Equity Offering

On June 11, 2015, the Company completed an equity offering to issue and sell 1,755 common shares for gross proceeds of $10,004 (the "Offering"). Proceeds net of commissions, legal, accounting and listing fees were $9,210. The Offering was carried out pursuant to an underwriting agreement with a syndicate of underwriters led by National Bank Financial Inc. and TD Securities Inc. and included Cormark Securities Inc., PI Financial Corp. and RBC Capital Markets.

Dividends

Dividends are payable in an equal amount on each common share if declared by the Board of Directors of the Company. No dividends were declared for the years ended December 31, 2016 and 2015.

15. Stock-Based Compensation

(a) Stock Options

There are 986 common shares reserved for issuance under the Company's stock option plan. Upon closing of the Company's initial public offering on June 26, 2007, 799 options granted under the Company's original option plan (the "Old Plan") fully vested. Options granted under the Old Plan expire 10 years from date of vesting and as at December 31, 2016, there are 63 (2015 – 115) options outstanding under the Old Plan with a weighted average exercise price of $4.00.

On June 18, 2007, the Company adopted a new option plan (the "2007 Option Plan") which is available to directors, officers, employees and other persons approved by the Board from time to time. On closing of the Company's initial public offering, 833 common shares were reserved for issuance under the 2007 Option Plan. The options granted under the 2007 Option Plan expire 10 years from the date of grant and vest on a quarterly basis in 12 equal amounts

over three years. All options under the 2007 Option Plan will vest immediately on a change of control of the Company. As of December 31, 2016, there are 609 options outstanding under the 2007 option plan.

For the years ended December 31, 2016 and 2015, the Company recorded stock-based compensation related to stock options of $212 and $446, respectively.

A summary of the status of the Company's stock option plan as at December 31, 2016 and 2015 is presented below.

	2016		2015	
	Number of Options	Weighted Average Exercise Price	Number of Options	Weighted Average Exercise Price
Outstanding - January 1	684	$5.89	1,318	$7.03
Granted	40	$5.12	12	$6.25
Exercised	(46)	$4.00	(287)	$4.30
Forfeited / Expired	(6)	$5.00	(359)	$11.37
Outstanding - December 31	672	$5.99	684	$5.89
Exercisable	592	$6.05	470	$5.94

As at December 31, 2016, the range of exercise prices, the weighted average exercise price and the weighted average remaining contractual life are as follows:

	Options Outstanding			Options Exercisable	
Range of exercise prices	**Number outstanding**	**Weighted average remaining contractual life (years)**	**Weighted average exercise price**	**Number exercisable**	**Weighted average exercise price**
$4.00	63	0.49	$4.00	63	$4.00
$4.01 - $5.50	50	7.90	$5.11	17	$5.08
$5.51 - $11.50	513	7.08	$5.79	466	$5.79
$11.51 - $11.75	46	0.46	$11.75	46	$11.75
	672	5.82	$5.99	592	$6.05

The fair value of stock option grants made to directors during the year is estimated using the Black-Scholes option pricing model, with the following weighted average assumptions: risk-free rate of 1.08% (2015 – 1.58%); dividend yield of nil; volatility of 46.60% (2015 – 48.80%); and expected lives of stock options of 7.9 years (2015 – 7.9). Expected volatility has been based on an evaluation of the historical period commensurate with the expected term. The expected term of the stock options has been based on historical experience and general option holder behavior. The fair value of the stock options is expensed over the vesting period of the options using the graded method.

(b) Restricted Share Units (RSUs)

On March 12, 2009, the Company established a RSU Plan which is available to the directors, officers, and full-time employees approved by the Board. The value of one RSU is equal to the value of one Common Share. Plan participants are granted a specific number of RSUs for a given period based on their position and level of contribution. At the end of the three-year vesting period, the RSUs vest if the plan participant is employed by the Company. Vested RSUs are expected to be paid in cash or Common Shares purchased on the open market, or a combination of both, as the Company chooses.

For the year ended December 31, 2016 and December 31, 2015, the Company recorded compensation expense of $266 and $244, respectively, related to the RSUs granted. As of December 31, 2016, a liability of $707 (2015 - $441) related to the RSUs granted is included in other long-term liabilities (Note 11).

The following table is a summary of the number of outstanding RSU as at:

	December 31 2016	December 31 2015
Opening Balance, January 1	150	150
Granted	12	-
Vested	-	-
Ending Balance, December 31	162	150

(c) Performance-Based Share Units (PSUs)

Plan participants are granted a specific number of PSUs for a given period based on their role within the Company and level of performance. PSUs are also issued pursuant to the RSU Plan. At the end of the three-year vesting period, the PSUs vest if the plan participant is employed by the Company and certain non-market performance criteria are met. Vested PSUs are expected to be paid in cash or Common Shares purchased on the open market, or a combination of both, as the Company chooses. The PSUs are re-measured to fair value each reporting period. The value of one PSU is equal to the value of one Common Share.

In 2016, the Company granted 256 PSUs to certain executives (2015 – 153).

In 2016, 5 PSUs vested and the Company paid cash of $25 (2015 – nil).

For the year ended December 31, 2016 and December 31, 2015, the Company recorded stock-based compensation expense of $35 and $211, respectively, related to the PSUs outstanding. As at December 31, 2016, a liability of $318 (2015 - $309) related to the PSUs granted is included in the other long-term liabilities (Note 11).

The following table is a summary of the number of outstanding PSUs as at:

	December 31 2016	December 31 2015
Opening Balance, January 1	252	119
Granted	256	153
Exercised/ Vested	(5)	-
Forfeited/ Expired	(308)	(20)
Ending Balance, December 31	195	252

(d) Stock-Based Compensation Summary

The following table is a summary of the stock-based compensation expense.

	Year ended December 31 2016	Year ended December 31 2015
Restricted share units	$ 266	$ 244
Performance-based share units	35	211
Stock options	212	446
Directors' fees paid in shares	353	371
	$ 866	$ 1,272

16. Loss Per Share

The following table sets forth the calculation of basic and diluted loss per share.

	Year ended December 31 2016	Year ended December 31 2015
Numerator for basic and diluted loss per share:		
Net loss for the year	$ (4,314)	$ (2,810)
Denominator for basic and diluted loss per share:		
Basic weighted average number of shares outstanding	14,177	13,069
Effect of stock options, RSUs and PSUs	-	-
Diluted weighted average number of shares outstanding	14,177	13,069
Loss per share:		
Basic	$ (0.30)	$ (0.22)
Diluted	$ (0.30)	$ (0.22)

For the year ended December 31, 2016, the impact of all options, RSUs and PSUs totaling 1,223 (2015 – 1,086) were excluded in the calculation of diluted loss per share because they were antidilutive.

The comparative basic and diluted weighted average number of shares outstanding for the year ended December 31, 2015 have been corrected to 13,069 shares outstanding, due to an immaterial arithmetic error in the prior year financial statements. As a result, the basic and diluted earnings per share was adjusted from ($0.23) to ($0.22).

17. Revenue

The Company’s revenue is comprised of the following:

	Year ended December 31 2016	Year ended December 31 2015
Cloud and Colocation Revenue	$ 18,296	$ 13,166
Connectivity Revenue	40,790	44,554
	$ 59,086	$ 57,720

18. Key Management Personnel Compensation

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, including the directors of the Company.

Key management personnel compensation, including directors, is as follows:

		Year ended December 31 2016		Year ended December 31 2015
Salaries, fees and benefits	$	1,759	$	2,091
Termination expense		2,860		219
Share-based compensation expense		866		1,258
	$	5,485	$	3,568

19. Commitments

The Company is committed to leases for premises, office equipment, network real estate access, automobiles, telecommunication facilities and radio spectrum licenses. Annual minimum payments over the next five years and thereafter are as follows:

		Amount
2017	$	11,297
2018		8,938
2019		7,281
2020		4,261
2021		3,541
Thereafter		2,321
	$	37,639

For the year ended December 31, 2016, the Company recorded rent expense of $7,494 (2015 - $7,032) relating to premises and network real estate access leases.

It is common practice for the Company to re-negotiate network real estate access lease or license arrangements as they become due for renewal. Included in the amounts above are estimates for the renewal of leases or licenses that are currently due for renewal or are due for renewal in 2017.

The Company is required to pay, under a CRTC-administered regime, a percentage (2016 - 0.53%, 2015 – 0.56%) of its adjusted Canadian telecommunications service revenue (as defined by CRTC and excluding retail Internet revenue) into a fund administered by CRTC.

20. Fair value of financial instruments

The Company has determined the estimated fair values of its financial instruments based on appropriate valuation methodologies. Where quoted market values are not readily available, the Company may use considerable judgment to develop estimates of fair value. Accordingly, any estimated values are not necessarily indicative of the amounts the Company could realize in a current market exchange and could be materially affected by the use of different assumptions or methodologies. The Company classifies its fair value measurements within a fair value hierarchy, which reflects the significance of the inputs used in making the measurements as defined in IFRS 7 – Financial Instruments – Disclosures.

Level 1 - Unadjusted quoted prices in active markets for identical assets or liabilities;
Level 2 - Inputs other than quoted prices included in Level 1, that are observable for the asset or liability, either directly or indirectly; and
Level 3 - Unobservable inputs for the asset or liability which are supported by little or no market activity

The fair values of cash and cash equivalents, short-term investments and restricted cash, which are primarily money market and fixed income securities, are based on quoted market values. The fair values of short-term financial assets

and liabilities, including accounts receivable, accounts payable and accrued liabilities, as presented in the consolidated statements of financial position, approximate their carrying amounts due to their short-term maturities. The fair value of long-term debt approximates its carrying value because management believes the interest rates approximate the market interest rate for similar debt with similar security. The fair value of our interest rate swap contract is based on broker quotes and therefore, these contracts are measured using Level 2 inputs. Similar contracts are traded in an active market and the quotes reflect the actual transactions in similar instruments.

The Company has classified its financial instruments as follows:

	December 31 2016		December 31 2015	
	Carrying amount	Fair Value	Carrying amount	Fair Value
Financial assets:				
Loans and receivables, measured at amortized cost				
Cash and cash equivalents	$ 13,034	$ 13,034	$ 13,066	$ 13,066
Accounts receivable	3,673	3,673	3,306	3,306
Restricted cash	-	-	172	172
Financial liabilities:				
Accounts payable and accrued liabilities, measured at amortized cost	$ 11,027	$ 11,027	$ 9,128	$ 9,128
Fair value of interest rate swap contract	261	261	612	612
Long-term debt, measured at amortized cost	40,778	40,778	45,781	45,781

Credit risk

The Company's cash and cash equivalents and restricted cash subject the Company to credit risk. The Company maintains cash and investment balances at Tier 1 Canadian financial institutions. The Company's maximum exposure to credit risk is limited to the amount of cash and cash equivalents.

Credit risk related to our interest rate swap contract arises from the possibility that the counter party to the agreement may default on their obligation. The Company assesses the creditworthiness of the counterparty to minimize the risk of counterparty default. The interest rate swap is held by National Bank Financial.

The Company, in the normal course of business, is exposed to credit risk from its customers and the accounts receivable are subject to normal industry risks. The Company attempts to manage these risks by dealing with credit worthy customers. If available, the Company reviews credit bureau ratings, bank accounts and industry references for all new customers. Customers that do not have this information available are typically placed on a pre-authorized payment plan for service or provide deposits to the Company. This risk is minimized as the Company has a diverse customer base located across various provinces in Canada.

As at December 31, 2016 and 2015, the Company had no material past due trade accounts receivable. The following table provides the aging of the trade accounts receivable:

	December 31 2016	December 31 2015
Current	$ 2,597	$ 2,302
31 to 60 days	650	769
61 to 90 days	116	77
over 90 days	168	-
	$ 3,531	$ 3,148

Interest rate risk

The Company is subject to interest rate risk on its cash and cash equivalents and long-term debt. The Company is exposed to interest rate risk on its operating line of credit since the interest rates applicable are variable and is, therefore, exposed to cash flow risks resulting from interest rate fluctuations. As at December 31, 2016, the operating line of credit balance was $nil. The drawn term facility as at December 31, 2016 was $41,250, $41,100 of which was held in a Bankers Acceptance. In 2015, the Company entered into amended interest rate swap contracts that matures June 29, 2018. The interest rate on the Banker's Acceptance at December 31, 2016 was 3.99%. The remaining $150 drawn under this facility bears interest for the period at prime rate plus a margin.

Liquidity risk

The Company believes that its current cash and cash equivalents and anticipated cash from operations will be sufficient to meet its working capital and capital expenditure requirements for the foreseeable future. As at December 31, 2016, the Company had cash and cash equivalents of $13,034. The Company has access to the $34,345 undrawn portion of its $85,000 credit facilities after consideration of outstanding letters of credit.

The Company's financial liabilities that have contractual maturities are summarized below:

	Less than 1 year	2 - 3 years	Total
Long-term debt	$ 5,170	$ 35,608	$ 40,778
Accounts payable	3,025	-	3,025
Fair value of interest rate swap contract	-	261	261
Stock-based compensation[1]	723	302	1,025
Total	$ 8,918	$ 36,171	$ 45,089

[1] Represents recognized amounts for cash-settled stock-based compensation arrangements (See Note 15). Settlement is subject to achievement of vesting criteria.

Currency risk

The Company has suppliers that are not based in Canada which gives rise to a risk that earnings and cash flows may be adversely affected by fluctuations in foreign currency exchange rates. The Company is primarily exposed to the fluctuations in the dollar. The Company believes this risk is minimal and does not use financial instruments to hedge these risks. A one cent appreciation in the U.S. dollar to Canadian dollar foreign exchange rate would have resulted in a decrease (increase) in income of $6. Balances denominated in foreign currencies that are considered financial instruments are as follows:

	Currency	December 31 2016	December 31 2015
Cash and cash equivalents	USD	$ 275	$ 138
Accounts payable and accrued liabilities	USD	744	595

21. Capital Risk Management

The Company's objectives when managing capital are:

(a) to ensure that the Company will continue as a going concern so that it can continue to provide services to its customers and offer a return on investment to its shareholders;
(b) to maintain a capital structure which optimizes the cost of capital while providing flexibility and diversity of funding sources and timing of debt maturities along with adequate anticipated liquidity for future growth; and
(c) to comply with debt covenants

The Company defines capital that it manages as the aggregate of its cash and cash equivalents, short-term investments, debt facilities including finance leases and equity comprising of share capital, contributed surplus and deficit.

		December 31 2016		December 31 2015
Cash and cash equivalents	$	(13,034)	$	(13,066)
Long term debt		40,778		45,781
Share capital		86,171		85,636
Contributed surplus		25,620		25,408
Deficit		(63,143)		(58,829)
	$	76,392	$	84,930

The Company manages its capital structure and makes adjustments to it in light of economic conditions. The Company, upon approval from its Board of Directors, will make changes to its capital structure as deemed appropriate under the specific circumstances.

The Company's overall strategy with respect to management of capital remains unchanged from the year ended December 31, 2016.

22. Related Party Transactions

Two former Directors of the Company, who retired effective June 23, 2016, also served as Chairman of the Board and a Director of a customer of the Company. Revenue from this customer for the year ended December 31, 2016 and 2015 was $40 and $79, respectively. Accounts receivable from this customer as at December 31, 2016 and 2015 was nil and $3, respectively.

The terms governing these related party transactions are consistent with those negotiated on an arm's length basis with non-related parties.

CORPORATE INFORMATION

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Chief Operating Officer, ECN Capital Corp.

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Managing Partner, Second Alpha Partners

Antonio Ciciretto
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Chief Executive Officer, Rohinni LLC

Nicole German
Head of Marketing, SAP Canada

Jerry S. Grafstein, Q.C.
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Jim Sanger
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Gary Sherlock
Corporate Director

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YEAR END
December 31

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