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HUNGARIAN TELEPHONE & CABLE CORP

Form 10-Q

August 14, 2002

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2002 Commission file number 1-11484  
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HUNGARIAN TELEPHONE AND CABLE CORP.  
(Exact name of registrant as specified in its charter)

Delaware 13-3652685  
-----  
(State or other jurisdiction (I.R.S. Employer Identification No.)  
of incorporation or organization)

1201 Third Avenue, Suite 3400 Seattle, WA 98101-3034  
(Address of principal executive offices)

(206) 654-0204  
(Registrant's telephone number, including area code)

32 Center Street, Darien, CT 06820  
(Former Address)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past ninety days.

Yes X No  
-----

Indicate the number of shares outstanding of each of the issuer's classes of Common Stock as of the latest possible date:

Common Stock, \$.001 par value 12,103,180 Shares  
(Class) (Outstanding at August 13, 2002)

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## HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

### Table of Contents

Part I. Financial Information:	Page No. -----
Condensed Consolidated Balance Sheets	2
Condensed Consolidated Statements of Operations and Comprehensive Income	3
Condensed Consolidated Statements of Stockholders' Equity	4
Condensed Consolidated Statements of Cash Flows	5
Notes to Condensed Consolidated Financial Statements	6
Management's Discussion and Analysis of Financial Condition and Results of Operations	14
Quantitative and Qualitative Disclosures about Market Risk	26
 Part II. Other Information	 27
 Signatures	 29

- 1 -

## Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

### Item 1. Financial Statements Condensed Consolidated Balance Sheets (In thousands, except share data)

Assets -----	June 30, 2002 ----- (unaudited)	December 31, 2001 -----
Current assets:		
Cash and cash equivalents	\$ 9,950	\$ 9,262
Restricted cash	113	210
Accounts receivable, net	5,341	4,797
Other current assets	3,264	1,677
	-----	-----
Total current assets	18,668	15,946
Property, plant and equipment, net	110,616	100,971
Goodwill, less accumulated amortization	7,053	6,050
Other intangibles, less accumulated amortization	4,034	3,672
Deferred costs	6,396	6,652
Other assets	2,866	2,780
	-----	-----
Total assets	\$149,633 =====	\$136,071 =====

### Liabilities and Stockholders' Equity -----

Current liabilities:

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Current installments of long-term debt	\$ 16,382	\$ 12,311
Short-term loans	-	3,531
Accounts payable	574	1,015
Accruals	4,300	2,974
Other current liabilities	2,230	1,551
Due to related parties	433	957
	-----	-----
Total current liabilities	23,919	22,339
Long-term debt, excluding current installments	107,435	104,882
Deferred credits and other liabilities	8,425	8,484
	-----	-----
Total liabilities	139,779	135,705
	-----	-----
Commitments and Contingencies		
Stockholders' equity:		
Cumulative Convertible preferred stock, \$.01 par value; \$70.00 liquidation value. Authorized 200,000 shares; issued and outstanding 30,000 shares in 2002 and 2001	-	-
Common stock, \$.001 par value. Authorized 25,000,000 shares; issued and outstanding 12,103,180 shares in 2002 and 2001	12	12
Additional paid-in capital	144,744	144,706
Accumulated deficit	(150,046)	(159,151)
Accumulated other comprehensive income	15,144	14,799
	-----	-----
Total stockholders' equity	9,854	366
	-----	-----
Total liabilities and stockholders' equity	\$149,633	\$136,071
	=====	=====

See accompanying notes to condensed consolidated financial statements.

- 2 -

Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES  
Condensed Consolidated Statements of Operations and Comprehensive Income  
For the Three and Six Month Periods Ended June 30, 2002 and 2001  
(In thousands, except share and per share data)

(unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2002	2001	2002	2001
	-----	-----	-----	-----
Telephone service revenues, net	\$12,402	\$10,999	\$24,261	\$22,231
Operating expenses:				

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Operating and maintenance expenses	4,759	4,042	9,125	8,318
Depreciation and amortization	2,459	2,278	4,787	4,605
	-----	-----	-----	-----
Total operating expenses	7,218	6,320	13,912	12,923
	-----	-----	-----	-----
Income from operations	5,184	4,679	10,349	9,308
Other income (expenses):				
Foreign exchange gains, net	2,662	7,476	3,331	5,340
Interest expense	(2,423)	(3,430)	(4,966)	(7,095)
Interest income	142	364	413	778
Other, net	(3)	(3)	30	25
	-----	-----	-----	-----
Net income	\$ 5,562	\$ 9,086	\$ 9,157	\$ 8,356
Cumulative convertible preferred stock dividends in arrears)	(26)	(27)	(52)	(53)
	-----	-----	-----	-----
Net income ascribable to common stockholders	5,536	9,059	9,105	8,303
Comprehensive income adjustments	374	(545)	345	330
	-----	-----	-----	-----
Total comprehensive income	\$ 5,910	\$ 8,514	\$ 9,450	\$ 8,633
	=====	=====	=====	=====
Earnings per common share:				
Basic	\$ 0.46	\$ 0.75	\$ 0.75	\$ 0.69
	=====	=====	=====	=====
Diluted	\$ 0.44	\$ 0.72	\$ 0.73	\$ 0.66
	=====	=====	=====	=====
Weighted average number of common shares outstanding:				
Basic	12,103,180	12,103,180	12,103,180	12,096,760
	=====	=====	=====	=====
Diluted	12,590,695	12,567,788	12,522,230	12,600,935
	=====	=====	=====	=====

See accompanying notes to condensed consolidated financial statements.

- 3 -

Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES  
Condensed Consolidated Statements of Stockholders' Equity  
(In thousands, except share data)

(unaudited)

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	Shares	Common Stock	Preferred Stock	Additional Paid-In Capital	Accumulated deficit
Balances at December 31, 2001	12,103,180	\$ 12	-	144,706	(159,151)
Modification of option terms	-	-	-	38	-
Cumulative convertible preferred stock dividends (in arrears)	-	-	-	-	(52)
Net Income	-	-	-	-	9,157
Foreign currency translation adjustment	-	-	-	-	-
Balances at June 30 2002	12,103,180	\$ 12	-	144,744	(150,046)

See accompanying notes to condensed consolidated financial statements.

- 4 -

Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES  
Condensed Consolidated Statements of Cash Flows  
For the Six Month Periods Ended June 30, 2002 and 2001  
(In thousands)

(unaudited)

	2002	2001
Net cash provided by operating activities	\$10,517	\$ 5,089
Cash flows from investing activities:		
Construction of telecommunication networks	(1,526)	(2,263)
Decrease (increase) in construction deposits	48	(2,683)
Acquisition of minority interest in subsidiary	(14)	-
Proceeds from sale of assets	100	20
Net cash used in investing activities	(1,392)	(4,926)

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Cash flows from financing activities:		
Repayments of long-term debt	(5,875)	(3,291)
Repayments of short-term debt	(3,595)	-
Proceeds from exercise of stock options and pre-emptive rights	-	114
	-----	-----
Net cash (used in) provided by financing activities	(9,470)	(3,177)
	-----	-----
Effect of foreign exchange rate changes on cash	1,033	5
	-----	-----
Net increase (decrease) in cash and cash equivalents	688	(3,009)
Cash and cash equivalents at beginning of period	9,262	15,596
	-----	-----
Cash and cash equivalents at end of period	\$ 9,950	12,587
	=====	=====

See accompanying notes to condensed consolidated financial statements.

- 5 -

Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES  
Notes to Condensed Consolidated Financial Statements

(unaudited)

(1) Summary of Significant Accounting Policies  
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(a) Basis of Presentation

The accompanying condensed consolidated financial statements of Hungarian Telephone and Cable Corp. ("HTCC" or the "Registrant" and, together with its consolidated subsidiaries, the "Company") have been prepared without audit and, in the opinion of management, include all adjustments, consisting mainly of normal recurring accruals, necessary for a fair presentation. Results for interim periods are not necessarily indicative of the results for a full year.

The accompanying condensed consolidated financial statements include the financial statements of the Company and its majority owned subsidiaries: Hungarotel Tavkozlesi Rt. ("Hungarotel") (the "Operating Company") and Pilistav Rt. ("Pilistav"). Until December 31, 2001, the Company had four other operating subsidiaries in Hungary, which merged into Hungarotel as of that date. All material intercompany balances and transactions have been eliminated.

The accompanying condensed consolidated financial statements are prepared in accordance with U.S. generally accepted accounting principles (U.S. GAAP). In preparing financial statements in conformity with U.S. GAAP, management is required to make estimates and assumptions. These estimates and assumptions affect reported amounts of assets and liabilities and the disclosure of contingent assets and

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liabilities at the date of the financial statements, as well as revenues and expenses during the reporting period. Actual results could differ from those estimates.

The condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements of Hungarian Telephone and Cable Corp. and its subsidiaries for the year ended December 31, 2001, including the notes thereto, set forth in the Company's annual report on Form 10-K filed with the United States Securities and Exchange Commission ("SEC").

- 6 -

Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES  
Notes to Condensed Consolidated Financial Statements

(unaudited)

(b) Earnings Per Share

Earnings per share ("EPS") is computed by dividing income ascribable to common stockholders by the weighted average number of common shares outstanding for the period. Diluted EPS is computed similar to basic earnings per share, except that the weighted average shares outstanding are increased to include additional shares from the assumed exercise of stock options and warrants, and the conversion of the convertible preferred stock, where dilutive. The number of additional shares is calculated by assuming that outstanding stock options were exercised, or preferred securities were converted, and that the proceeds from such exercises or conversions were used to acquire shares of common stock at the average market price during the reporting period.

The following is a reconciliation from basic earnings per share to diluted earnings per share for the three and six month periods ended June 30, 2002 and 2001:

	3 Months Ended		6 Months
	2002	2001	2002
(\$ in thousands, except share data)			
Net income ascribable to common stockholders (A)	\$ 5,536	\$ 9,059	\$ 9,105
plus: preferred stock dividends	26	27	52
	\$ 5,562	\$ 9,086	\$ 9,157
Determination of shares:			
Weighted average common shares outstanding - basic (C)	12,103,180	12,103,180	12,103,180
Assumed conversion of dilutive stock options and			

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cumulative convertible preferred stock	487,515	464,608	419,050
	-----	-----	-----
Weighted average common shares outstanding - diluted (D)	12,590,695	12,567,788	12,522,230
Net income per common share:			
Basic (A/C)	\$0.46	\$0.75	\$0.75
Diluted (B/D)	\$0.44	\$0.72	\$0.73

- 7 -

Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES  
Notes to Condensed Consolidated Financial Statements

(unaudited)

For the three and six month periods ended June 30, 2002, 2,639,400 and 2,825,400 stock options and warrants, respectively, and for the three and six month periods ended June 30, 2001, 2,934,400 and 2,889,400 stock options and warrants, respectively, were excluded from the computation of diluted earnings per share since such options and warrants have an exercise price in excess of the average market value of the Company's common stock during the period.

(c) Foreign Exchange Financial Instruments

Foreign exchange financial instrument contracts are utilized by the Company to manage certain foreign exchange rate risks. Company policy prohibits holding or issuing derivative financial instruments for trading purposes.

(d) Foreign Currency Translation

Since commencement of revenue generating activities, the Company has used the Hungarian forint as the functional currency for its Hungarian subsidiaries. Accordingly, foreign currency assets and liabilities are translated using the exchange rates in effect at the balance sheet date. Results of operations are generally translated using the average exchange rates for the period. The translation of the subsidiaries' forint denominated accounts into U.S. dollars, as of June 30, 2002, has been affected by the strengthening of the Hungarian forint against the U.S. dollar from 279.03 as of December 31, 2001 to 246.72 as of June 30, 2002, an approximate 13% appreciation in value.

(2) Cash and Cash Equivalents

(a) Cash

At June 30, 2002, cash of \$3,204,000 comprised the following: \$475,000 on deposit in the United States, and \$2,729,000 consisting of \$202,000 denominated in U.S. dollars, the equivalent of \$92,000 denominated in euros and the equivalent of \$2,435,000 denominated in Hungarian forints



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on deposit with banks in Hungary.

### (b) Cash Equivalents

Cash equivalents amounted to approximately \$6,746,000 at June 30, 2002 and consisted of Hungarian government securities, denominated in Hungarian forints, purchased under agreements to resell which mature within three months.

- 8 -

### Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES Notes to Condensed Consolidated Financial Statements

(unaudited)

### (3) Related Parties

Amounts due to related parties totalling \$433,000 at June 30, 2002 is comprised of the following: \$333,000 due to a subsidiary of Citizens Communications Company, representing cumulative preferred stock dividends in arrears, and \$100,000 representing payments due to three former officers under separate termination, consulting and non-competition agreements. The Company paid approximately \$604,000, in the aggregate, during each of the six month periods ended June 30, 2002 and 2001 to the former officers under these agreements.

### (4) Segment Disclosures

The Company operates in a single industry segment, telecommunications services. The Company has constructed a modern telecommunications infrastructure in order to provide a full range of the Company's products and services in its five concession areas in Hungary. While the Company's chief operating decision maker monitors the revenue streams of the various products and services, operations are managed and financial performance is evaluated based on the delivery of multiple services to customers over an integrated network. Substantially all of the Company's assets are located in Hungary and all of its operating revenues are generated in Hungary.

#### Products and Services

The Company groups its products and services into the following categories:

Telephone Services - local dial tone and switched products and services that provide incoming and outgoing calls over the public switched network. This category includes reciprocal compensation revenues and expenses (i.e. interconnect).

Network Services - point-to-point dedicated services that provide a private transmission channel for the Company's customers' exclusive use between two or more locations, both in local and long distance applications.

Other Service and Product Revenues - PBX hardware sales and service revenues, as well as miscellaneous other telephone service revenues.

- 9 -

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Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES  
Notes to Condensed Consolidated Financial Statements

(unaudited)

The revenues generated by these products and services for the periods ended June 30 were as follows:

	3 Months Ended		6 Months Ended	
	2002	2001	2002	2001
	----	----	----	----
(\$ in thousands)				
Telephone services	\$11,166	\$10,144	\$21,880	\$20,53
Network services	860	622	1,674	1,24
Other service and product revenues	376	233	707	45
	-----	-----	-----	-----
	\$ 12,402	\$10,999	\$24,261	\$22,23
	=====	=====	=====	=====

### Major Customers

For the periods ended June 30, 2002 and 2001, none of the Company's customers accounted for more than 10% of the Company's total revenues.

### (5) Derivative Instruments and Hedging Activities

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The Company applies the provisions of Statement of Financial Accounting Standards No. 133 ("SFAS 133"), "Accounting for Derivative Instruments and Hedging Activities", as subsequently amended by Statement of Financial Accounting Standards No. 138 ("SFAS 138") in its financial statements. Accordingly, the Company carries its foreign currency forward contracts at fair value in its consolidated balance sheet. The fair value is based on forward rates provided by the counterparty bank with which the Company has entered into the forward contract. The foreign currency forward contracts the Company has entered into do not qualify for hedge accounting, as defined under SFAS 133 and 138, and, accordingly, changes in the fair value of the forward contracts are reported in the consolidated statement of operations and comprehensive income, as a part of net foreign exchange gains (losses).

The fair value of the Company's foreign currency forward contracts at December 31, 2001 was approximately \$6,000. The Company did not have open foreign currency forward contracts at June 30, 2002.

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HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES  
Notes to Condensed Consolidated Financial Statements

(unaudited)

### (6) Goodwill, Intangible and Other Long-Lived Assets

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On January 1, 2002 the Company adopted Statement of Financial Accounting Standard No. 142 ("SFAS 142"), "Goodwill and Other Intangible Assets," which establishes new accounting and reporting standards for acquired goodwill and other intangible assets and supersedes APB Opinion No. 17. Goodwill and intangible assets that have indefinite useful lives will no longer be amortized but rather will be tested at least annually for impairment. Intangible assets that have finite useful lives (whether or not acquired in a business combination) will continue to be amortized over their useful lives, which are no longer limited to a maximum of 40 years.

The Company recorded amortization expense related to goodwill of approximately \$107,000 and \$214,000 for the three and six month periods ended June 30, 2001, respectively. The adoption of the provisions of SFAS 142 has eliminated the goodwill charge in 2002. Intangible assets, which consist of concession rights, have finite lives and continue to be amortized over the twenty-five year concession period using the straight-line method.

During the first quarter of 2002, the Company performed the first step of the required SFAS No. 142 impairment test, with respect to goodwill, as of January 1, 2002. This first step required the Company to compare the carrying value of any reporting unit that has goodwill to the estimated fair value of the reporting unit. If the current fair value was less than the carrying value, then the Company would perform the second step of the impairment test. This second step would require the Company to measure the excess of the recorded goodwill over the current value of the goodwill, and to record any excess as an impairment. The Company completed step one during the first quarter of 2002, and based upon the results, the Company concluded that there is no impairment to the carrying value of goodwill reported in its financial statements.

On January 1, 2002, the Company adopted SFAS No. 144 ("SFAS 144"), "Accounting for Impairment or Disposal of Long-Lived Assets," which establishes a single accounting method for long-lived assets to be disposed of by sale and broadens the presentation of discontinued operations. The guidance in SFAS 144, with regard to the impairment of long-lived assets held for use, is substantially consistent with SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," except that goodwill is subject to impairment testing under SFAS 142. The adoption of this statement had no impact on the Company's results of operations or financial position.

- 11 -

Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES  
Notes to Condensed Consolidated Financial Statements

(unaudited)

### (7) Commitments and Contingencies - Legal Proceedings

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During 1996 and 1997, Hungarotel entered into several construction contracts

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with a Hungarian contractor, which totaled \$59.0 million in the aggregate, \$47.5 million of which was financed by a contractor financing facility. By January 1998, it became clear to Hungarotel that there were problems with the work undertaken by the contractor and Hungarotel rejected invoices in the amount of approximately HUF 700 million (approximately \$2.8 million at June 30, 2002 exchange rates) for, among other reasons, the contractor's failure to meet the contractual capacity requirements and breaches of warranties regarding the quality of work. During 1998, the Company and the contractor engaged in settlement discussions in order to resolve these issues but were unable to reach a settlement. Following a series of transactions in March 1999 with the contractor's major creditor, Hungarotel acquired a HUF 3.1 billion (approximately \$12.6 million at June 30, 2002 exchange rates) net claim against the contractor, at the same time settling, through legal offset, the contractor's claims arising from accepted but unpaid invoices in the amount of HUF 900 million (approximately \$3.6 million at June 30, 2002 exchange rates). These transactions were undertaken to strengthen Hungarotel's position in any potential procedures initiated by the contractor. The contractor is seeking payment under separate invoices in the amount of approximately \$24 million for work which the Company is disputing because of quality and quantity issues. The Company still has claims against the contractor of approximately \$31 million which is more than the contractor's claim.

In July 2001, the contractor filed an additional lawsuit challenging certain transactions regarding litigated matters between the contractor's creditor and the Company. A hearing was held on this matter in April 2002 in the Metropolitan Court in Budapest, Hungary. At this hearing, the judge ordered the parties to file some documents supporting their claims with the Court. Following the filing of these documents, a new court hearing will be scheduled for later this year. The Company believes that this additional lawsuit is without merit and that the Company will prevail.

In December 1999, a debt collection company initiated debt collection proceedings against the Hungarian contractor for non-payment of various debts. In June 2000, the debt collection company claimed the benefit of certain invoices that the contractor had issued to Hungarotel in the amount of HUF 455 million (approximately \$1.8 million at June 30, 2002 exchange rates), stating that the contractor had assigned those invoices to it "as security" in the debt collection proceedings. Hungarotel rejected the debt collection company's claim for, among other reasons, the absence of a right

- 12 -

Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES  
Notes to Condensed Consolidated Financial Statements

(unaudited)

by the contractor to assign the invoices and that, in any event, Hungarotel has a substantive defense and counterclaim on the merits to the underlying claim on the invoices. After a court hearing in November 2001, the debt collection company reduced its claim against Hungarotel to HUF 250 million (approximately \$1.0 million at June 30, 2002 exchange rates) (and proportionally reduced the amount of interest claimed) because it could not substantiate the HUF 455 million claim on the basis of the contractor's assignment agreement. At a further hearing in December 2001, the court terminated the proceedings, on the grounds that it had no jurisdiction to deal with the matter because the terms of the contract between Hungarotel and the contractor stated that disputes surrounding the contract are to be resolved through arbitration proceedings. The debt collection company

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successfully appealed to the Hungarian Supreme Court against this decision and the matter has been remitted to the lower court, but no date for the next substantive hearing has yet been set. The Company believes that it will prevail.

Papatel, one of the Company's pre-merger operating subsidiaries, was involved in a dispute with the Hungarian taxing authorities (the "APEH") pursuant to which the APEH alleged that Papatel owed HUF 107 million (approximately \$434,000 at June 30, 2002 exchange rates). This amount included late payment penalties and default interest on value added tax ("VAT"), which the APEH alleged should have been charged in 1999 to the Ministry by Papatel when Papatel relinquished its rights to use broadcasting frequencies previously granted by the Ministry. A court hearing was held in March 2002, at which, the matter was suspended for at least six months. The suspension was granted because the matter had concurrently been referred to the Principal Tax Administration Department of the Ministry of Finance. By its order made on June 25, 2002, the Principal Tax Administration Department quashed the APEH resolutions establishing the alleged VAT shortfall. As a result of this, it is expected that the APEH will issue a formal resolution bringing the dispute to an end and that the court proceedings will be terminated.

- 13 -

### Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

#### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

##### Introduction

Hungarian Telephone and Cable Corp. ("HTCC" or the "Registrant" and, together with its consolidated subsidiaries, the "Company") is engaged primarily in the provision of telecommunications services through its operating subsidiary, Hungarotel Tavkozlesi Rt. ("Hungarotel"). Until December 31, 2001, the Company had four other operating subsidiaries in Hungary, which merged into Hungarotel as of that date. The Company earns substantially all of its telecommunications revenue from measured service fees, monthly line rental fees, connection fees, public pay telephone services and ancillary services (including charges for additional services purchased at the customer's discretion).

Since commencing the provision of telecommunications services in 1995, the Company's network construction and expansion program has added approximately 141,000 access lines through June 30, 2002 to the approximately 61,000 access lines acquired directly from Magyar Tavkozlesi Rt. ("Matav"), the former State-controlled monopoly telephone company. During the late 1990's, the development and installation of the network in each of the Company's operating areas required significant capital expenditures.

The Company achieved EBITDA1 of \$7.6 million during the quarter ended June 30, 2002, up from EBITDA of \$7.0 million for the quarter ended June 30, 2001. Now that the Company's networks are built-out, the ability of the Company to generate sufficient revenues to satisfy cash requirements and maintain profitability will depend upon a number of factors, including the Company's ability to attract additional customers both within and outside its operating areas and increased revenues per customer. These factors are expected to be primarily influenced by the success of the Company's operating and marketing strategies, as well as market acceptance of telecommunications services both within and outside the Company's operating areas. In addition, the Company's profitability may be affected by changes in the Company's regulatory environment

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and other factors that are beyond the Company's control.

The Company's results and financial position, reported in U.S. dollars, continues to be significantly affected by movements in the Hungarian forint/U.S. dollar exchange rate.

EBITDA is defined, by the Company, as net revenue less operating and maintenance expenses. The Company has included information concerning EBITDA because it uses EBITDA and understands that it is used by certain investors as one measure of a company's ability to service or incur indebtedness. EBITDA is not a measure of financial performance under U.S. generally accepted accounting principles and is not necessarily comparable to similarly titled measures used by other companies. EBITDA should not be construed as an alternative to operating or net income, or to cash flows from operating activities (as determined in accordance with U.S. generally accepted accounting principles).

- 14 -

### Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

#### Critical Accounting Policies

The Company's discussion and analysis of its financial condition and results of operations are based upon its consolidated financial statements which have been prepared in accordance with generally accepted accounting principles in the United States ("US GAAP"). This preparation requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses, and the disclosure of contingent assets and liabilities. US GAAP provides the framework from which to make these estimates, assumption and disclosures. The Company chooses accounting policies within US GAAP that management believes are appropriate to accurately and fairly report the Company's operating results and financial position in a consistent manner. Management regularly assesses these policies in light of current and forecasted economic conditions. The accounting policies the Company believes to be critical to understanding the results of operations and the effect of the more significant judgments and estimates used in the preparation of the condensed consolidated financial statements are the same as those described in its Annual Report on Form 10-K for the year ended December 31, 2001.

In addition to those described in the Company's Annual Report on Form 10-K for the year ended December 31, 2001, the Company believes the following accounting policy is critical to understanding the results of operations and the effect of the more significant judgments and estimates used in the preparation of its condensed consolidated financial statements:

Goodwill - In 2002, and annually thereafter, the Company will assess the fair value of goodwill. To the extent that information indicates that the carrying amount of the Company's net assets exceed the Company's estimated fair value, the Company will recognize an impairment charge. During the first quarter of 2002, the Company performed its impairment testing with respect to goodwill, as of January 1, 2002, and based upon the results, the Company concluded that there is no impairment to the carrying value of goodwill reported in its financial statements. The Company's estimates of fair value will be subject to revision as market conditions change.

Comparison of Three Months Ended June 30, 2002 and Three Months Ended June 30, 2001

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The Company's Hungarian subsidiaries functional currency is the Hungarian forint. The average Hungarian forint/U.S. dollar exchange rate for the three months ended June 30, 2002 was 264.50, as compared to an average Hungarian forint/U.S. dollar exchange rate for the three months ended June 30, 2001 of 294.57. When comparing the three months ended June 30, 2002 to the three months ended June 30, 2001, it should be noted that all U.S. dollar reported amounts have been affected by this 11% appreciation in the Hungarian subsidiaries' functional currency.

- 15 -

### Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

#### Net Revenues

	Quarter Ended June 30		
(dollars in millions)	2002	2001	% change
Measured service revenues	7.4	7.1	4
Subscription revenues	4.9	4.0	23
Net interconnect charges	(1.8)	(1.6)	(13)
	----	----	
Net measured service and subscription revenues	10.5	9.5	11
Connection fees	0.6	0.5	20
Other operating revenues, net	1.3	1.0	30
	----	----	
Telephone Service Revenues, Net	12.4	11.0	13
	====	====	

The Company recorded a 13% increase in net telephone service revenues to \$12.4 million for the three months ended June 30, 2002 from \$11.0 million for the three months ended June 30, 2001.

Net measured service and subscription revenues increased 11% to \$10.5 million for the three months ended June 30, 2002 from \$9.5 million for the three months ended June 30, 2001. Measured service revenues increased 4% to \$7.4 million during the three months ended June 30, 2002 from \$7.1 million during the three months ended June 30, 2001. Subscription revenues increased 23% to \$4.9 million during the three months ended June 30, 2002 from \$4.0 million during the three months ended June 30, 2001. Measured service revenues decreased in functional currency terms by approximately 7% as a result of a decrease in average access lines in service from approximately 205,600 for the three months ended June 30, 2001 to approximately 202,300 during the three months ended June 30, 2002, and lower minutes of use for some telecommunications services. Due to economic conditions and pricing issues, both within and outside the Company's operating areas, the Company has not opted to raise call tariffs on most of its calling services effective July 1, 2002, although it was allowed to do so by the Hungarian regulatory authority. Subscription revenues increased in functional currency terms by approximately 12% as a result of (i) an approximate 4% increase in monthly subscription fees and (ii) the revenues associated with the Company becoming a Universal Service Provider during the period. As a Universal Service Provider the Company will receive funds from a Hungarian government fund established to provide (i) country-wide access to fixed line telecommunications services at reasonable prices, (ii) public pay telephones, (iii) operator assisted services, and (iv) free emergency services. The funds to be received by the Company are based upon the number of customers, which meet certain

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requirements defined in government regulations.

These revenues have been reduced by net interconnect charges which totalled \$1.8 million for the three months ended June 30, 2002 compared to \$1.6 million for the three months ended June 30, 2001. As a percentage of measured

- 16 -

### Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

service and subscription revenues, net interconnect charges have remained consistent at approximately 14% for each of the three month periods ended June 30, 2002 and 2001.

#### Operating and Maintenance Expenses

Operating and maintenance expenses increased 18% to \$4.8 million for the three months ended June 30, 2002, as compared to \$4.0 million for the three months ended June 30, 2001. In functional currency terms, operating and maintenance expenses of Hungarotel increased approximately 2% for the three months ended June 30, 2002, as compared to the three months ended June 30, 2001. In U.S. dollar terms, however, the increase in such costs in functional currency terms has been magnified by the 11% appreciation of the Hungarian forint. There has also been an increase in the Company's U.S. dollar denominated operating expenses, between the periods.

#### Depreciation and Amortization

Depreciation and amortization charges increased \$0.2 million to \$2.5 million for the three months ended June 30, 2002 from \$2.3 million for the three months ended June 30, 2001. Depreciation and amortization charges of Hungarotel decreased in functional currency terms by approximately 3% due to the adoption of SFAS 142, which requires the amortization of goodwill to cease effective January 1, 2002. However, this decrease has been offset by the 11% appreciation of the Hungarian forint between the periods. Included in depreciation and amortization charges for the three months ended June 30, 2001 is approximately \$0.1 million of amortization relating to goodwill.

#### Income from Operations

Income from operations increased to \$5.2 million for the three months ended June 30, 2002 from \$4.7 million for the three months ended June 30, 2001. Contributing to such improvement were higher net telephone service revenues offset by higher operating and maintenance expenses and slightly higher depreciation and amortization charges.

#### Foreign Exchange Gains

Foreign exchange gains amounted to \$2.7 million for the three months ended June 30, 2002, compared to \$7.5 million for the three months ended June 30, 2001. The foreign exchange gains for the three months ended June 30, 2002 resulted primarily from the effect of the appreciation of the Hungarian forint against the U.S. dollar on the Company's 25 million U.S. dollar denominated debt outstanding during the period. At June 30, 2002, the Hungarian forint had appreciated in value by approximately 13% against the U.S. dollar, and was consistent against the euro, as compared to March 31, 2002 levels. The foreign exchange gains for the three months ended June 30, 2001 resulted primarily from the effect of the appreciation of the Hungarian forint on the Company's U.S. dollar 25 million and euro 88 million denominated debt during that period.



- 17 -

Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

At June 30, 2001, the Hungarian forint had appreciated in value by approximately 9% against the euro and approximately 5% against the U.S. dollar as compared to March 31, 2001 levels. Included in foreign exchange gains for the three months ended June 30, 2002 is approximately \$0.2 million of foreign exchange losses relating to the Company's closed foreign currency forward contracts. When non-Hungarian forint debt is re-measured into Hungarian forints, the Company reports foreign exchange gains/losses in its consolidated financial statements as the Hungarian forint appreciates/devalues against such non-forint currencies. See the "Inflation and Foreign Currency" and "Market Risk Exposure" sections below.

Interest Expense

Interest expense decreased 29% to \$2.4 million for the three months ended June 30, 2002 from \$3.4 million for the three months ended June 30, 2001. This \$1.0 million decrease is attributable to lower interest rates paid on the Company's borrowings, as well as lower average debt levels outstanding between the periods. The Company's weighted average interest rate on the Company's debt obligations went from 8.92% for the three months ended June 30, 2001, to 6.52% for the three months ended June 30, 2002, a 27% decrease. See "Liquidity and Capital Resources" section below.

Interest Income

Interest income decreased to \$0.1 million for the three months ended June 30, 2002, from \$0.4 million for the three months ended June 30, 2001, due to lower interest rates on Hungarian forint deposits, as well as lower average cash balances between the periods.

Net Income

As a result of the factors discussed above, the Company recorded net income ascribable to common stockholders of \$5.5 million, or \$0.46 per share, or \$0.44 per share on a diluted basis, for the three months ended June 30, 2002 as compared to \$9.1 million, or \$0.75 per share, or \$0.72 per share on a diluted basis, during the three months ended June 30, 2001.

Comparison of Six Months Ended June 30, 2002 to Six Months Ended June 30, 2001  
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As previously mentioned, the Company's Hungarian subsidiaries functional currency is the Hungarian forint. The average Hungarian forint/U.S. dollar exchange rate for the six months ended June 30, 2002 was 271.47, as compared to an average Hungarian forint/U.S. dollar exchange rate for the six months ended June 30, 2001 of 291.12. When comparing the six months ended June 30, 2002 to the six months ended June 30, 2001, it should be noted that all U.S. dollar

- 18 -

Part I. Financial Information  
HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

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reported amounts have been affected by this 7% appreciation in the Hungarian subsidiaries' functional currency.

### Net Revenues

	Year-to-date		
(dollars in millions)	2002	2001	% change
Measured service revenues	14.5	14.5	-
Subscription revenues	9.5	7.9	20
Net interconnect charges	(3.4)	(3.2)	(6)
	----	----	
Net measured service and subscription revenues	20.6	19.2	7
Connection fees	1.2	1.1	9
Other operating revenues	2.5	1.9	32
	----	----	
Telephone Service Revenues, Net	24.3	22.2	9
	=====	=====	

The Company recorded a 9% increase in net telephone service revenues of \$24.3 million for the six months ended June 30, 2002 as compared to revenues of \$22.2 million for the six months ended June 30, 2001.

Net measured service and subscription revenues increased 7% to \$20.6 million for the six months ended June 30, 2002 from \$19.2 million for the six months ended June 30, 2001. Measured service revenues remained consistent at \$14.5 million, while subscription revenues increased 20% to \$9.5 million for the six months ended June 30, 2002. Measured service revenues decreased in functional currency terms by approximately 7% as a result of (i) a decrease in average access lines in service from approximately 206,100 for the six months ended June 30, 2001 to approximately 202,800 during the six months ended June 30, 2002, (ii) lower minutes of use for some telecommunications services, and (iii) a slight decrease in call tariffs between the periods. Due to economic conditions and pricing issues, both within and outside the Company's operating areas, the Company has not opted to raise call tariffs on most of its calling services effective July 1, 2002, although it was allowed to do so by the Hungarian regulatory authority. Subscription revenues increased in functional currency terms by approximately 13% as a result of (i) an approximate 4% increase in monthly subscription fees and (ii) the revenues associated with the Company becoming a Universal Service Provider during the period. As a Universal Service Provider the Company will receive funds from a Hungarian government fund established to provide (i) country-wide access to fixed line telecommunications services at reasonable prices, (ii) public pay telephones, (iii) operator assisted services, and (iv) free emergency services. The funds to be received by the Company are based upon the number of customers, which meet certain requirements defined in government regulations.

- 19 -

### Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

These revenues have been reduced by net interconnect charges which totalled

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\$3.4 million for the six months ended June 30, 2002 compared to \$3.2 million for the six months ended June 30, 2001. As a percentage of measured service and subscription revenues, net interconnect charges have remained consistent at approximately 14% for each of the six month periods ended June 30, 2002 and 2001.

### Operating and Maintenance Expenses

Operating and maintenance expenses increased 10% to \$9.1 million for the six months ended June 30, 2002, as compared to \$8.3 million for the six months ended June 30, 2001. In functional currency terms, operating and maintenance expenses of Hungarotel increased approximately 1% for the six months ended June 30, 2002, as compared to the six months ended June 30, 2001. In U.S. dollar terms, however, the increase in such costs in functional currency terms has been magnified by the 7% appreciation of the Hungarian forint. There has also been an increase in the Company's U.S. dollar denominated operating expenses, between the periods.

### Depreciation and Amortization

Depreciation and amortization charges increased \$0.2 million to \$4.8 million for the six months ended June 30, 2002 from \$4.6 million for the six months ended June 30, 2001. Depreciation and amortization charges of Hungarotel decreased in functional currency terms by approximately 3% due to the adoption of SFAS 142, which requires the amortization of goodwill to cease effective January 1, 2002. However, this decrease has been offset by the 7% appreciation of the Hungarian forint between the periods. Included in depreciation and amortization charges for the six months ended June 30, 2001 is approximately \$0.2 million of amortization relating to goodwill.

### Income from Operations

Income from operations increased to \$10.3 million for the six months ended June 30, 2002 compared to \$9.3 million for the six months ended June 30, 2001. Contributing to such improvement were higher net telephone service revenues offset by higher operating and maintenance expenses and slightly higher depreciation and amortization charges.

### Foreign Exchange Gains

Foreign exchange gains amounted to \$3.3 million for the six months ended June 30, 2002, compared to \$5.3 million for the six months ended June 30, 2001. The foreign exchange gains for the six months ended June 30, 2002 resulted primarily from the effect of the appreciation of the Hungarian forint on the

- 20 -

## Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

Company's average EUR 75.1 million and U.S. dollar 25 million denominated debt outstanding during the period. At June 30, 2002, the Hungarian forint had appreciated in value by approximately 1% against the euro, and by approximately 13% against the U.S. dollar as compared to December 31, 2001 levels. The foreign exchange gains for the six months ended June 30, 2001 resulted primarily from the effect of the appreciation of the Hungarian forint on the Company's euro 88 million denominated debt during that period. At June 30, 2001, the Hungarian forint appreciated in value by approximately 8% against the euro as compared to December 31, 2000 levels. Included in foreign exchange gains for the six months

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ended June 30, 2002 is approximately \$0.2 million of foreign exchange losses relating to the Company's closed foreign currency forward contracts. When non-Hungarian forint debt is re-measured into Hungarian forints, the Company reports foreign exchange gains/losses in its consolidated financial statements as the Hungarian forint appreciates/devalues against such non-forint currencies. See the "Inflation and Foreign Currency" and "Market Risk Exposure" sections below.

### Interest Expense

Interest expense decreased 30% to \$5.0 million for the six months ended June 30, 2002 from \$7.1 million for the six months ended June 30, 2001. This \$2.1 million decrease is attributable to lower interest rates paid on the Company's borrowings, as well as lower average debt levels outstanding between the periods. The Company's weighted average interest rate on the Company's debt obligations went from 8.99% for the six months ended June 30, 2001, to 6.67% for the six months ended June 30, 2002, a 26% decrease. See "Liquidity and Capital Resources" section below.

### Net Income

As a result of the factors discussed above, the Company recorded net income ascribable to common stockholders of \$9.1 million, or \$0.75 per share, or \$0.73 per share on a diluted basis, for the six months ended June 30, 2002 as compared to \$8.3 million, or \$0.69 per share, or \$0.66 per share on a diluted basis, for the six months ended June 30, 2001.

### Liquidity and Capital Resources

The Company has historically funded its capital requirements primarily through a combination of debt, equity and vendor financing. The ongoing development and installation of the network in each of the areas in which the Company operates required significant capital expenditures (\$198.5 million at historical exchange rates through June 30, 2002). Since the end of 1998, the Company's networks have had the capacity, with only normal additional capital

- 21 -

## Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

expenditure requirements, to provide basic telephone services to virtually all of the potential subscribers within the areas in which it operates.

Net cash provided by operating activities totalled \$10.5 million during the six months ended June 30, 2002 compared to \$5.1 million during the six months ended June 30, 2001. The significant increase in net cash provided by operating activities between the two periods is primarily due to (i) a decrease of approximately \$3 million in the amount of interest paid on the Company's debt obligations in 2002, as compared to 2001, due to a change in the dates when interest was paid in 2001, (ii) lower average interest rates and (iii) improved working capital movements in 2002, as compared to 2001. For the six months ended June 30, 2002 and 2001, the Company used \$1.4 million and \$4.9 million, respectively, in investing activities, which was primarily used to fund additions to the Company's telecommunications networks. Financing activities used net cash of \$9.5 million during the six months ended June 30, 2002 compared to \$3.2 million for the six months ended June 30, 2001. The cash used by financing activities was for the scheduled repayments of the Company's short-term and long-term debt obligations.

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On April 11, 2000, the Company entered into an EUR 130 million Senior Secured Debt Facility Agreement (the "Debt Agreement") with a European banking syndicate. The Company drew down EUR 129 million of the Facility on April 20, 2000 (\$121 million at historical exchange rates). As of June 30, 2002, the Company has repaid approximately \$22.9 million, at historical exchange rates, of the original EUR 129 million drawn down. The Company believes that its current cash flow will allow it to meet its working capital needs, including its obligations under the Debt Agreement.

The Company's major contractual cash obligations as disclosed in its December 31, 2001 Form 10-K filing have not materially changed as of June 30, 2002. The Company's ability to generate sufficient cash flow from operations to meet its contractual cash obligations is subject to many factors, including regulatory developments, competition and customer behavior and acceptance of additional fixed line telecommunications services. Under the Company's Debt Agreement, the Company must maintain certain levels of earnings before interest, foreign exchange gains/losses, taxes, depreciation and amortization and cash flow in order to comply with its debt covenant ratios as set out in the Debt Agreement. Until March 31, 2002, the ratios were calculated based on the Company's U.S. dollar consolidated financial statements. With effect from June 30, 2002, the ratios are calculated based on the Company's U.S. dollar consolidated financial statements translated into euros. This exposes the Company to the possible risk of not meeting its debt covenant ratios, as measured in euro terms, due to the effect of currency movements on translation of its Hungarian forint denominated assets, liabilities, revenues and expenses

- 22 -

### Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

into euros. While management seeks to manage the business to be in compliance with its Debt Agreement and related covenants, management operates in a regulated environment which is subject to many factors outside of its control (i.e. the ruling government party's political, social and public policy agenda). The Company's liquidity may also be affected by exchange rate fluctuations due to approximately 72% of its debt not being denominated in Hungarian forints. The Company attempts to reduce this exchange rate risk, however, through the use of forward hedging contracts.

#### Inflation and Foreign Currency

In May 2001, the National Bank of Hungary widened the trading band the Hungarian forint is allowed to trade within from +/- 2.25% of the mid-point of the band to +/- 15%. This widening caused the Hungarian forint to initially appreciate in value against the euro by approximately 4%. Subsequent to the band widening, and without any notice, in June 2001 the National Bank of Hungary lifted all remaining foreign exchange restrictions concerning the Hungarian forint, thus making the Hungarian forint fully and freely convertible. With the widening of the trading band, the potential volatility of the Hungarian forint has increased, as is evidenced by prior quarters exchange rate gains and losses. See the "Market Risk Exposure" section below.

The Company's Hungarian operations generate revenues in Hungarian forints and incur operating and other expenses, including capital expenditures, predominately in Hungarian forints but also in U.S. dollars and euros. In addition, certain of the Company's balance sheet accounts are denominated in currencies other than the Hungarian forint, the functional currency of the

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Company's Hungarian subsidiaries. Accordingly, when such accounts are translated into Hungarian forints, the Company is subject to foreign exchange gains and losses which are reflected as a component of net income. When the subsidiaries' forint-denominated financial statements are translated into U.S. dollars for financial reporting purposes, the Company is subject to translation adjustments, the effect of which is reflected as a component of stockholders' equity.

While the Company has the ability to increase the prices it charges for its services commensurate with increases in the Hungarian Consumer Price Index ("CPI") pursuant to its licenses from the Hungarian government, and as regulated by the government, it may choose not to implement the full amount of the increase permitted due to competitive and other concerns. In addition, the rate of increase in the Hungarian CPI may not be sufficient to offset potential negative exchange rate movements and as a result, the Company may be unable to generate cash flows to the degree necessary to meet its obligation in currencies other than the Hungarian forint.

- 23 -

### Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

#### Market Risk Exposure

The Company is exposed to various types of risk in the normal course of its business, including the impact of foreign currency exchange rate fluctuations and interest rate changes. Company operations, including all revenues and approximately 87% of operating expenses are Hungarian forint based and are therefore subject to exchange rate variability between the Hungarian forint and the U.S. dollar. Due to the lifting of all foreign exchange restrictions concerning the Hungarian forint in May 2001, and the volatility in euro/U.S. dollar exchange rates, Hungarian forint/euro and Hungarian forint/U.S. dollar exchange rate variability has increased. This increase in variability is evident by the fact that the Hungarian forint/U.S. dollar exchange rate went from 279.03 as of December 31, 2001 to 246.72 as of June 30, 2002, an approximate 13% appreciation in value of the Hungarian forint versus the U.S. dollar. At the same time, the Hungarian forint/euro exchange rate went from 246.33 as of December 31, 2001 to 244.67 as of June 30, 2002, an approximate 1% appreciation in value of the Hungarian forint versus the euro.

The debt obligations of the Company are Hungarian forint, euro and U.S. dollar denominated. The interest rate on the Hungarian forint debt obligations is based on the Budapest Bank Offer Rate (BUBOR). The interest rates on the euro and U.S. dollar denominated obligations are based on EURIBOR and USD LIBOR, respectively. Over the medium to long term, the BUBOR rate is expected to follow inflation and devaluation trends and the Company does not currently believe it has any material interest rate risk on any of its Hungarian forint denominated debt obligations. If a 1% change in the BUBOR interest rate were to occur, the Company's interest expense would increase or decrease by approximately \$0.4 million annually based upon the Company's June 30, 2002 debt level. If a 1% change in EURIBOR interest rates were to occur, the Company's interest expense would increase or decrease by approximately \$0.7 million annually based upon the Company's June 30, 2002 debt level. If a 1% change in USD LIBOR interest rates were to occur, the Company's interest expense would increase or decrease by approximately \$0.3 million annually based upon the Company's June 30, 2002 debt level.

The Company is exposed to exchange rate risk insofar as the Company has

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debt obligations in currencies other than the functional currency of its Hungarian subsidiaries. Given the Company's debt obligations, which include euro and U.S. dollar denominated debt, if a 5% change in Hungarian forint/euro exchange rates were to occur, the Company's euro denominated debt, in U.S. dollar terms, would increase or decrease by approximately \$3.5 million, based upon the Company's June 30, 2002 debt level. If a 5% change in Hungarian forint/U.S. dollar exchange rates were to occur, the Company's foreign exchange rate gain would increase or decrease by approximately \$1.3 million based on Hungarotel's U.S. dollar denominated borrowings from HTCC as of June 30, 2002.

- 24 -

### Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

The Company utilizes foreign currency forward contracts or purchases foreign currencies in advance to reduce its exposure to exchange rate risks associated with cash payments in euro maturing within six months under the Company's long-term debt obligations. The forward contracts establish the exchange rates at which the Company will sell the contracted amount of Hungarian forints for euros at a future date. The Company utilizes forward contracts which are six months in duration and at maturity will either receive or pay the difference between the contracted forward rate and the exchange rate at the settlement date. The Company did not have any open foreign currency forwards at June 30, 2002. The counterparties to the Company's foreign currency forward contracts are substantial and creditworthy multinational commercial banks which are recognized market makers. The risk of counterparty nonperformance associated with these contracts is not considered by the Company to be material.

#### Recent Accounting Pronouncements

On January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 141, "Business Combinations" (SFAS 141) and Statement No. 142, "Goodwill and Other Intangible Assets" (SFAS 142). SFAS 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001. SFAS 141 also provides new criteria to determine whether an acquired intangible asset should be recognized separately from goodwill. Under SFAS 142, the Company ceased to amortize goodwill effective January 1, 2002. As required by SFAS 142, the Company reassessed the expected useful lives of existing intangible assets, which resulted in no change.

During the first quarter of 2002, the Company performed the first step of the required SFAS 142 impairment test, with respect to goodwill, as of January 1, 2002. This first step required the Company to compare the carrying value of any reporting unit that has goodwill to the estimated fair value of the reporting unit. If the current fair value was less than the carrying value, then the Company would perform the second step of the impairment test. This second step would require the Company to measure the excess of the recorded goodwill over the current value of the goodwill, and to record any excess as an impairment. The Company completed step one during the first quarter of 2002, and based upon the results, the Company concluded that there is no impairment to the carrying value of goodwill reported in its financial statements.

In April 2002, the Financial Accounting Standards Board ("FASB") issued SFAS No. 145 ("SFAS 145"), "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections". SFAS 145 provides for the rescission of several previously issued accounting standards, new accounting guidance for the accounting for certain lease modifications and

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various technical corrections that are not substantive in nature to existing

- 25 -

### Part I. Financial Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

pronouncements. SFAS 145 will be adopted beginning January 1, 2003, except for the provisions relating to the amendment of SFAS No. 13, which will be adopted for transactions occurring subsequent to May 15, 2002. Management is assessing the impact, if any, this Statement may have on its consolidated results of operations or financial position.

On July 30, 2002, the FASB issued SFAS No. 146 ("SFAS 146"), "Accounting for Costs Associated with Exit or Disposal Activities". SFAS 146 nullifies Emerging Issues Task Force Issue No. 94-3 ("EITF Issue No. 94-3"), "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)". SFAS 146 requires that a liability for a cost associated with an exit or disposal activity should be recorded when it is incurred and initial measurement be at fair value. The statement is effective for exit or disposal activities that are initiated after December 31, 2002, although earlier adoption is encouraged.

#### Strategic Market Expansion Efforts

With the Hungarian telecommunications market continuing to become more competitive, the Company is increasing its efforts to explore ways to increase the Company's market presence within Hungary. However, there can be no assurance that the Company will achieve its growth objectives.

#### Forward-Looking Statements

This report and other oral and written statements made by the Company to the public contain and incorporate by reference forward-looking statements as that term is defined in the Private Securities Litigation Reform Act of 1995. These statements are not predictions, but rather are, statements of expectations, estimates and current plans as they currently exist, and are constantly under review by the Company. For these statements, the Company claims the protection of the safe harbor for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995. These forward-looking statements involve risks, uncertainties and assumptions and such statements are qualified by important factors that may cause actual results to differ materially from those expressed in the forward-looking statements.

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

The information required by this Item is contained under the heading "Market Risk Exposure" under Item 2. "Management's Discussion and Analysis of Financial Condition and Results of Operations."

- 26 -

### Part II. Other Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES



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### Item 1. Legal Proceedings

As reported in Item 3. "Legal Proceedings" in the Company's Report on Form 10-K for the year ended December 31, 2001, the Company is involved in legal proceedings with Fazis, a Hungarian contractor. As reported in the Company's Report on Form 10-K, Reorg Rt. ("Reorg"), a company responsible for collecting Fazi's creditor's debts, had initiated a proceeding against the Company claiming the benefit of certain invoices that Fazi's issued to the Company. The Metropolitan Court of Budapest dismissed Reorg's claims based on jurisdictional grounds and ruled that the claim should be decided by arbitration proceedings. Reorg appealed the Metropolitan Courts decision to the Hungarian Supreme Court and won. The Hungarian Supreme Court remitted the matter back to the Metropolitan Court.

### Item 2. Changes in Securities and Use of Proceeds

None

### Item 3. Default Upon Senior Securities

- (a) None.
- (b) On May 12, 1999, the Company issued 30,000 shares of Preferred Stock Series A with a liquidation value of \$70 per share to a subsidiary of Citizens Communications Company. Any holder of such Preferred Shares is entitled to receive cumulative cash dividends payable in arrears at the annual rate of 5%, compounded annually, on the liquidation value. As of June 30, 2002, the total arrearage on the Preferred Shares was \$333,000.

### Item 4. Submission of Matters to a Vote of Security Holders

- (a) The Annual Meeting of Stockholders of the Registrant was held on May 22, 2002.
- (b) Not Applicable.
- (c) First Matter Voted on at the Annual Meeting of Stockholders of the Registrant: Election of Directors

	Votes Cast For	Votes Withheld
	-----	-----
Ole Bertram	11,467,285	32,201
Daryl A. Ferguson	11,392,583	106,903
Thomas Gelting	11,491,975	7,511
Torben V. Holm	11,492,000	7,486
John B. Ryan	11,392,638	106,848
William E. Starkey	11,392,638	106,848
Leonard Tow	11,358,818	140,668

- 27 -

## Part II. Other Information

### HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

Second Matter Voted on at the Annual Meeting of Stockholders of the Registrant: Approval of the proposal to amend the Registrant's Incentive Stock Option Plan to extend the termination date of the plan from April 30, 2003 to April 30, 2008 and rename the plan, the "2002 Incentive Stock Option Plan".

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For	Against	Abstain	Not Voted
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9,269,452	74,507	32,900	2,122,627

Third Matter Voted on at the Annual Meeting of Stockholders of the Registrant: Ratification of the appointment of KPMG Hungaria Kft. as auditors of the Registrant for the fiscal year ending December 31, 2002.

For	Against	Abstain
---	-----	-----
11,496,351	1,310	1,825

(d) Not Applicable.

### Item 5. Other Information

In July 2002, Hungarian Telephone and Cable Corp. moved its U.S. office from 32 Center Street, Darien, CT to 1201 Third Avenue, Suite 3400, Seattle, WA 98101-3034. Its new telephone number is (206)-654-0204. The Company's subsidiary offices in Hungary have not changed.

### Item 6. Exhibits and Reports on Form 8-K

#### (a) Exhibit Description

- 2 Plan of acquisition, reorganization, arrangement, liquidation or succession (None)
- 3(i) Certificate of Incorporation of the Registrant, as amended, filed as Exhibit 4.1 to the Registrant's Registration Statement on Form S-8 filed on January 31, 2001 (File #333-54688) and incorporated herein by reference
- 3(ii) By-laws of the Registrant, as amended, filed as Exhibit 4.2 to the Registrant's Registration Statement on Form S-8 filed on January 31, 2001 (File #333-54688) and incorporated herein by reference
- 4.1 Specimen Common Stock Certificate, filed as Exhibit 4(a) to the Registrant's Registration Statement on Form SB-2 filed on October 27, 1994 and incorporated herein by reference (File #33-80676)

- 28 -

### Part II. Other Information HUNGARIAN TELEPHONE AND CABLE CORP. AND SUBSIDIARIES

- 4.2 Certificate of Designation of Series A - Preferred Stock of Hungarian Telephone and Cable Corp., filed as Exhibit 4.1 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended March 31, 1999 and incorporated herein by reference
- 11 Statement re computation of per share earnings (not required)
- 15 Letter re unaudited interim financial information (not required)

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- 18 Letter re change in accounting principles (none)
- 19 Report furnished to security holders (none)
- 22 Published report regarding matters submitted to vote of security holders (not required)
- 24 Power of Attorney (not required)
- 99.1 Certificate of Chief Executive Officer and Principal Financial Officer

(b) Reports on Form 8-K

None.

Signatures

Pursuant to the requirements of the Securities and Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Hungarian Telephone and Cable Corp.

August 13, 2002 By: /s/Ole Bertram  
Ole Bertram  
Chief Executive Officer and President

August 13, 2002 By: /s/William McGann  
William McGann  
Principal Accounting Officer,  
Principal Financial Officer, Controller  
and Treasurer

- 29 -

Hungarian Telephone and Cable Corp.

Index to Exhibits

Exhibit No.	Description
99.1	Certificate of Chief Executive Officer and Principal Financial Officer

EXHIBIT 99.1

HUNGARIAN TELEPHONE AND CABLE CORP.

CERTIFICATE OF CHIEF EXECUTIVE OFFICER AND PRINCIPAL FINANCIAL OFFICER

I, Ole Bertram, President and Chief Executive Officer of Hungarian Telephone and Cable Corp., certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

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To the best of my knowledge and belief, based upon a review of this quarterly report on Form 10-Q of Hungarian Telephone and Cable Corp. for the quarterly period ended June 30, 2002, and, except as corrected or supplemented in a subsequent report:

this quarterly report of Hungarian Telephone and Cable Corp. on Form 10-Q for the quarterly period ended June 30, 2002 which this statement accompanies fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

the information contained in this quarterly report on Form 10-Q of Hungarian Telephone and Cable Corp. for the quarterly period ended June 30, 2002 fairly presents, in all material respects, the financial condition and results of operations of Hungarian Telephone and Cable Corp.

By: /s/Ole Bertram  
-----  
Ole Bertram  
August 13, 2002

I, William T. McGann, Controller and Treasurer of Hungarian Telephone and Cable Corp., certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

To the best of my knowledge and belief, based upon a review of this quarterly report on Form 10-Q of Hungarian Telephone and Cable Corp. for the quarterly period ended June 30, 2002, and, except as corrected or supplemented in a subsequent report:

this quarterly report of Hungarian Telephone and Cable Corp. on Form 10-Q for the quarterly period ended June 30, 2002 which this statement accompanies fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

the information contained in this quarterly report on Form 10-Q of Hungarian Telephone and Cable Corp. for the quarterly period ended June 30, 2002 fairly presents, in all material respects, the financial condition and results of operations of Hungarian Telephone and Cable Corp.

By: /s/William T. McGann  
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William T. McGann  
August 13, 2002