# TOWER PROPERTIES COMPANY AND SUBSIDIARIES

## DISCLOSURE FOR FISCAL YEAR ENDED DECEMBER 31, 2016

**TOWER PROPERTIES COMPANY**
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For Online Access of Quarterly and Annual Disclosure Reports: otcmarkets.com Symbol: TPRP

**DIRECTORS**

Jonathan M. Kemper
Non-Executive Chairman of Tower Properties Company, Vice Chairman, Commerce Bancshares, Inc., a bank holding company, Vice Chairman, Commerce Bank, a Missouri Banking Corporation

Thomas R. Willard
President and Chief Executive Officer of Tower Properties Company, Vice Chairman of Commerce Trust Company, a division of Commerce Bank, a Missouri Banking Corporation

David W. Kemper
Chairman and Chief Executive Officer, Commerce Bancshares, Inc., a bank holding company, Chairman and Chief Executive Officer, Commerce Bank, a Missouri Banking Corporation

William E. Quirk
Attorney and Shareholder, Polsinelli PC, a law firm

John W. Kemper
President and Chief Operating Officer, Commerce Bancshares, Inc., a bank holding company, President, Commerce Bank, a Missouri Banking Corporation

**OFFICERS**

Thomas R. Willard
President and Chief Executive Officer

Stanley J. Weber
Chief Financial Officer, Chief Operating Officer, Vice President, Treasurer and Secretary

Margaret V. Schroeder
Vice President, Asst. Secretary and Controller

Christopher B. Erdley
Vice President

**General Development of Business**:

In September 1989, Tower Properties Company ("Tower") formed Tower Acquisition Corp. ("TAC"), a wholly-owned subsidiary of Tower. TAC was formed pursuant to the terms of a merger between Tower and Commerce Bancshares, Inc. ("Commerce"), a bank holding company. Tower spun off certain assets and liabilities to TAC with a net book value of approximately $17,500,000. Tower then merged with Commerce on January 29, 1990. In connection with the merger, each Tower shareholder received 7.88 shares of Commerce in exchange for each Tower share. TAC's capital stock was distributed to Tower's shareholders on January 29, 1990 in the form of a stock dividend. TAC's name was changed to Tower Properties Company ("the Company") on this same date. The net assets distributed to TAC represent the origination of the assets currently owned and managed by the Company.

A private letter ruling was obtained from the IRS that the distribution was tax-free under Section 355 of the Internal Revenue Code and the merger constituted a tax-free reorganization under Section 368(a)(1)(A) of the Internal Revenue Code.

**Description of the Company's Business**

The Company is primarily engaged in the business of owning, developing, leasing and managing real property. All real estate assets are located in Douglas and Johnson Counties in Kansas, and St. Louis County in Missouri. Substantially all the improved real estate owned by the Company consists of office buildings, apartment complexes, a warehouse/office facility and land held for future sale or development. The Company has not pursued a policy of acquiring real estate on a speculative basis for future sale, although some real estate owned by the Company may be sold at some future time.

The Company's leasing operations provided rental income constituting approximately 57 percent of the 2016 revenues. The remaining 43 percent of 2016 revenues include management and service fees (2 percent), gain on sales of assets (39 percent) and interest and other income (2 percent). The Company competes with other building owners in the renting and leasing of office building space and apartment housing. The Company employed 55 persons on a full-time basis and 7 persons on a part-time basis at December 31, 2016.

The Company leases rental space and parking and provides services to Commerce Bancshares, Inc. and its affiliates. The annual aggregate rental and service fees paid to the Company by Commerce will vary depending upon the space occupied and services provided. For the years ended December 31, 2016 and 2015, the Company received parking and fees of $811,831 and $968,633, respectively, from Commerce. The Company was also reimbursed by Commerce for labor and construction costs initially funded by the Company on behalf of Commerce in the amount of $5,118,474 and $9,241,647 in 2016 and 2015, respectively.

**Liquidity and Capital Resources**

The principal source of funds generated internally is income from operations. The principal source of external funds are long-term debt and a $13,500,000 loan ("Line of Credit") with Commerce Bank, a Missouri banking Corporation. The Line of Credit was renewed on June 1, 2016 and is collateralized by 257,759 shares of Commerce Bancshares, Inc. common stock and the warehouse/office facility at 9200

Cody. The warehouse/office facility at 9200 Cody was added as additional collateral for the Line of Credit on February 19, 2016. At December 31, 2016, the Company had no outstanding borrowings on the Line of Credit. The Company had $13,500,000 available under the Line of Credit at December 31, 2016. The Company does not utilize off-balance sheet financing.

Management believes that the Company's current combination of liquidity, capital resources and borrowing capabilities will be adequate for its existing operations during fiscal 2017. The Company did not experience liquidity problems during the year ended December 31, 2016. The Company does not anticipate any deficiencies in meeting its near term liquidity needs. The availability under the Line of Credit along with cash provided from operations is expected to give the Company adequate resources to meet the Company's cash requirements for 2017. If necessary, the Company believes it has adequate resources to collateralize additional financing. The Company had cash and cash equivalents of $1,641,000 at December 31, 2016. The Company's revenues are primarily based on lease contracts, none of which are deemed to be materially at risk.

**Real Property Owned by Company**

The Company considers all our properties to be in investment grade condition.

The Barkley Place, a 6-story 98,000 rentable square foot office building located in Overland Park, Kansas. The building was completed in 1988. The Company purchased the building on July 15, 1994. The building is presently 78 percent leased. The building is subject to a mortgage deed of trust securing a loan with a balance owing of $5,975,769 at December 31, 2016.

7911 Forsyth, a 6-story 55,000 rentable square foot office building with covered parking on five levels plus surface parking on top of the attached garage located in Clayton, Missouri. The building was completed in 1985. The Company purchased the building on December 1, 1998. The building is presently 95 percent leased. The building is subject to a mortgage deed of trust securing a loan with a balance owing of $6,696,280 at December 31, 2016.

Woodlands Plaza I, a 3-story 93,500 rentable square foot office building with surface parking for 348 cars located at 11720 Borman Drive, St. Louis, Missouri. The building was built in 1981 and renovated in 1998. The Company purchased the building on December 29, 2000. The building is presently 100 percent leased to a single tenant under a lease expiring in 2018. The building is subject to a mortgage deed of trust securing a loan with a balance owing of $2,510,602 at December 31, 2016.

6601 College Boulevard, a 6-story 99,000 rentable square foot office building, located in Overland Park, Kansas. The building was completed in 1979. The Company purchased the building on December 15, 1995. The building was fully renovated in 2016. It was previously leased to a single tenant under a triple net lease that expired on December 31, 2015. The building is presently vacant. The building is subject to a mortgage deed of trust securing a loan with a balance owing of $1,000,000 at December 31, 2016.

A warehouse/office facility, located at 9200 Cody, Overland Park, Kansas. The building contains approximately 49,000 square feet of office space and 71,900 square feet of warehouse space. The building was constructed in 1973, with an addition in 1976 and an expansion completed in 1997. In 2010 the building was renovated, which included some of the warehouse space being converted to office space. The Company purchased the facility on June 30, 1995. The building is presently 100 percent leased to a single tenant under a triple net lease expiring in 2024. The warehouse/office facility is collateral for the Line of Credit.

The One and Two Liberty Plaza buildings, two 2-story office buildings totaling approximately 54,000 square feet and surrounding surface parking lots located in Liberty, Missouri. Building One was completed in 1981 and Building Two was completed in 1984. The Company purchased the buildings on March 2, 2005. The buildings are presently 100 percent leased to a single tenant under a triple net lease expiring in 2025. The buildings are subject to a mortgage deed of trust securing a loan with a balance owing of $1,950,269 at December 31, 2016.

The 10955 Lowell Building (Building 20), a 10-story 112,000 square foot office building located in Overland Park, Kansas. The building was completed in 1983. The Company purchased the building on July 1, 2005. The building is presently 97 percent leased. The building is subject to a mortgage deed of trust securing a loan with a balance owing of $6,863,199 at December 31, 2016.

The 7400 Place Building, a 2-story 47,000 rentable square foot office building with a total of 177 parking spaces, 36 of which are in a one-story basement parking structure located at 7400 State Line, Prairie Village, Kansas. The building was completed in 1986. The Company purchased the building on December 15, 2006. The building is presently 100 percent leased. The building is subject to a mortgage deed of trust securing a loan with a balance owing of $3,030,699 at December 31, 2016.

The Corinth Office Building, a 2-story, above ground plus a lower level office building totaling 48,000 rentable square feet with a total of 140 surface parking spaces, located at 8340 Mission Road, Prairie Village, Kansas. The building was completed in 1965. The Company purchased the building on June 20, 2008. The building is presently 85 percent leased. The Corinth Executive Building, a 2-story 50,000 rentable square foot office building with a total of 235 surface parking spaces located at 4121 W. 83rd Street, Prairie Village, Kansas. The building was completed in 1973. The Company purchased the building on June 20, 2008. The building is presently 96 percent leased. The Somerset Building, a 2-story 43,000 rentable square foot office building with a total of 180 surface parking spaces located at 4200 Somerset, Prairie Village, Kansas. The building was completed in 1978. The Company purchased the building on June 20, 2008. The building is presently 93 percent leased. These three buildings are subject to a mortgage deed of trust securing a loan with a balance owing of $5,712,045 at December 31, 2016.

The Indian Creek Campus I Building, a 4-story 112,000 rentable square foot office building with a total of 490 parking spaces located at 10740 Nall, Overland Park, Kansas. The building was completed in 1998. The Company purchased the building on November 1, 2016. The building is presently 93 percent leased. The building is subject to a mortgage deed of trust securing a loan with a balance owing of $9,971,171 at December 31, 2016.
The Creekview Corporate Center Building, a 4-story 122,000 rentable square foot office building with a total of 570 parking spaces located at 12900 Foster, Overland Park, Kansas. The building was

completed in 1998. The Company purchased the building on November 1, 2016. The building is presently 100 percent leased. The building is subject to a mortgage deed of trust securing a loan with a balance owing of $10,469,456 at December 31, 2016.

The Company has approximately 30 acres of undeveloped land held for sale located in Kansas City North, Missouri, near the New Mark apartment complex owned by the Company. The tract is owned in fee.

A 24-building, 329-unit apartment complex, on a 30.3-acre tract, located at 5401 Fox Ridge Drive in Mission, Kansas called Hillsborough. Construction of the initial complex was completed in 1985, with an addition of 7 buildings in 1996. The Company purchased the complex on December 31, 1992. The apartments are presently 97 percent leased. The 329 units are subject to a mortgage deed of trust securing a loan with a balance owing of $18,455,935 at December 31, 2016.

A 12-building, 262-unit apartment complex, on a 14.34-acre tract located at 6800 Antioch in Merriam, Kansas called Peppertree. Construction of the initial complex was completed in 1987, with an addition of 100 units in 2009. The Company purchased the initial complex on September 30, 1993. The apartments are presently 98 percent leased. The initial 162 apartments are subject to a mortgage deed of trust securing a loan with a balance owing of $2,509,125 at December 31, 2016. The 100 apartments added in 2009 are subject to a mortgage deed of trust securing a loan with a balance owing of $4,991,141 at December 31, 2016.

A 6-building, 51-unit apartment complex, on a 3.1-acre tract, located at 2201 Harper Street in Lawrence, Kansas called Harper Square. Construction of the initial 4-building complex was completed in 1994, with an addition of 2 buildings in 2003. The Company purchased the complex on June 30, 2011. The apartments are presently 96 percent leased. The 51 units are subject to a mortgage deed of trust securing a loan with a balance owing of $1,399,898 at December 31, 2016.

A 111-building, 212-unit apartment complex, on a 35.6-acre tract, located at 3401 Hutton Drive in Lawrence, Kansas called Hutton Farms. Construction of the complex was completed in 2004. The Company purchased the complex on June 30, 2011. The apartments are presently 96 percent leased. The 212 units are subject to a mortgage deed of trust securing a loan with a balance owing of $17,796,538 at December 31, 2016.

A 45-building, 87-unit expansion of the Hutton Farms Apartment complex on a 16.415 acre tract, located in Lawrence Kansas adjacent to Hutton Farms. The Company purchased the land on September 1, 2015. Construction of the complex was completed in 2016. The apartments are presently 22 percent leased. The 87 units are subject to a mortgage deed of trust securing a loan with a balance of $7,460,336 at December 31, 2016.

A 16-building, 148-unit apartment complex, on a 9.6-acre tract, located at 2600 W. 6th St. in Lawrence, Kansas called Tuckaway. Construction of the initial 15-building complex was completed in 1997, with an addition of 1 building in 2004. The Company purchased the complex on June 30, 2011. The apartments are presently 95 percent leased. The 148 units are subject to a mortgage deed of trust securing a loan with a balance owing of $7,152,605 at December 31, 2016.

A 9-building, 49-unit apartment complex, on a 4.3-acre tract, located at 4241 Briarwood Drive in Lawrence, Kansas called Briarwood. Construction of the complex was completed in 2002. The Company purchased the complex on June 30, 2011. The apartments are presently 96 percent leased. The 49 units are subject to a mortgage deed of trust securing a loan with a balance owing of $2,449,822 at December 31, 2016.

A 35-building, 263-unit apartment complex, on a 22.7-acre tract, located at 7110 Lackman Road and 7150 Lackman Road in Shawnee, Kansas called Tuckaway at Shawnee. Construction of the initial 17-building complex was completed in 1999, with an addition of 18 buildings in 2000. The Company purchased the complex on November 1, 2012. The apartments are presently 98 percent leased. The 263 units are subject to a mortgage deed of trust securing a loan with a balance owing of $15,886,646 at December 31, 2016.

A 7-building, 208-unit apartment complex, on a 14.9-acre tract, located at 19501 W. 102nd Street in Lenexa, Kansas called Dunes at Falcon Valley Apartments. Construction of the complex was completed in 2008. The Company purchased the complex on May 13, 2014. The apartments are presently 90 percent leased. The 208 units are subject to a mortgage deed of trust securing a loan with a balance owing of $16,927,303 at December 31, 2016.

**PRINCIPAL REAL ESTATE OWNED BY**
**TOWER PROPERTIES COMPANY AND SUBSIDIARIES**

| | |
|---|---|
| Barkley Place Building | 6-story office building, 10561 Barkley<br>Overland Park, Kansas |
| 7911 Forsyth Office Building | 6-story office building and parking garage<br>Clayton, Missouri |
| Woodlands Plaza I Office Building | 3-story office building, 11720 Borman Drive<br>St. Louis, Missouri |
| 6601 College Boulevard Office Building | 6-story office building<br>Overland Park, Kansas |
| 9200 Cody Warehouse/Office Facility | 120,900 square foot warehouse/office facility<br>Overland Park, Kansas |
| One and Two Liberty Plaza Office Buildings | Two 2-story office buildings<br>Liberty, Missouri |
| 10955 Lowell (Building 20) Office Building | 10-story office building<br>Overland Park, Kansas |
| 7400 Place Office Building | 2-story office building, 7400 State Line<br>Prairie Village, Kansas |
| Corinth Office Building | 2-story office building, 8340 Mission Road<br>Prairie Village, Kansas |
| Corinth Executive Office Building | 2-story office building, 4121 W. 83rd Street<br>Prairie Village, Kansas |
| 4200 Somerset Office Building | 2-story office building<br>Prairie Village, Kansas |
| Indian Creek Campus I Office Building | 4-story office building, 10740 Nall<br>Overland Park, Kansas |
| Creekview Corporate Center Office Building | 4-story office building, 12900 Foster<br>Overland Park, Kansas |
| New Mark Subdivision | 30 acres of residential and commercial<br>land in the area of 100th and North Oak Streets<br>Kansas City, Missouri |
| Hillsborough Apartment Complex | 329 apartments located at 5401 Fox Ridge Drive<br>Mission, Kansas |
| Peppertree Apartment Complex | 262 apartments located at 6800 Antioch<br>Merriam, Kansas |
| Harper Square Apartment Complex | 51 apartments located at 2201 Harper St.<br>Lawrence, Kansas |
| Hutton Farms Apartment Complex | 299 apartments located at 3401 Hutton Drive<br>Lawrence, Kansas |

| | |
|---|---|
| Tuckaway Apartment Complex | 148 apartments located at 2600 W. 6th St<br>Lawrence, Kansas |
| Briarwood Apartment Complex | 49 apartments located at 4241Briarwood Drive<br>Lawrence, Kansas |
| Tuckaway at Shawnee Complex | 263 apartments located at 7110 & 7150 Lackman Road<br>Shawnee, Kansas |
| Dunes at Falcon Valley Complex | 208 apartments located at 19501 W. 102nd Street<br>Lenexa, Kansas |

All of the real estate is located in Douglas and Johnson Counties in Kansas and St. Louis County in Missouri.

**TOWER PROPERTIES COMPANY & SUBSIDIARIES**
**CONSOLIDATED BALANCE SHEETS**
**December 31, 2016 and December 31, 2015**

| **ASSETS** | **2016** | **2015** |
|---|---|---|
| Investment in Commercial Properties: | | |
| Rental Property, Net | $ 180,833,532 | $ 147,301,254 |
| Tenant Leasehold Improvements, Net | 5,240,121 | 5,109,223 |
| Equipment and Furniture, Net | 9,891,574 | 8,664,849 |
| Construction in Progress | 55,203 | 5,494,221 |
| Commercial Properties, Net | 196,020,430 | 166,569,547 |
| | | |
| Real Estate Held for Sale | 135,157 | 135,157 |
| | | |
| Cash and Cash Equivalents (Related Party) | 1,640,825 | 13,205,980 |
| Investment Securities At Fair Value (Related Party) | 14,901,048 | 10,442,932 |
| Receivables (Including Related Party) | 1,683,339 | 2,279,808 |
| Income Taxes Recoverable | 603,657 | 552,167 |
| Prepaid Expenses and Other Assets | 1,241,185 | 1,236,259 |
| Intangible Asset-Acquired In-Place Leases Value | 1,270,000 | -- |
| Intangible Asset-Acquired Above-Market Leases | 204,800 | -- |
| **Total Assets** | $ 217,700,441 | $ 194,421,850 |
| | | |
| **LIABILITIES AND STOCKHOLDERS' INVESTMENT** | | |
| Liabilities: | | |
| Mortgage Notes | $ 149,208,839 | $ 144,400,550 |
| Unamortized Debt Issuance Costs | (908,928) | (978,430) |
| Accounts Payable and Other Liabilities | 7,128,923 | 6,663,913 |
| Deferred Income Taxes | 21,978,927 | 12,358,649 |
| Total Liabilities | 177,407,761 | 162,444,682 |
| | | |
| Commitments and Contingencies | | |
| | | |
| Stockholders' Investment: | | |
| Preferred Stock, No Par Value | | |
| Authorized 2,000 Shares, None Issued | -- | -- |
| Common Stock, Par Value $1.00 | | |
| Authorized 33,334 Shares, Issued | | |
| 6,181 Shares | 6,181 | 6,181 |
| Paid-In Capital | 19,108,978 | 19,108,978 |
| Retained Earnings | 31,369,457 | 18,755,395 |
| Accumulated Other Comprehensive Income | 8,562,881 | 5,843,431 |
| | 59,047,497 | 43,713,985 |
| | | |
| Less Treasury Stock, At Cost (1,980 and | | |
| 1,395 shares in 2016 and 2015, respectively) | (18,754,817) | (11,736,817) |
| Total Stockholders' Investment | 40,292,680 | 31,977,168 |
| **Total Liabilities and Stockholder's Investment** | $ 217,700,441 | $ 194,421,850 |

See accompanying notes to the consolidated financial statements.

**TOWER PROPERTIES COMPANY & SUBSIDIARIES**
**CONSOLIDATED STATEMENTS OF OPERATIONS**
**FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015**

| | 2016 | 2015 |
|---|---|---|
| **REVENUES** | | |
| Non-Related Party Revenues: | | |
| Rent | $ 31,198,608 | $ 33,003,153 |
| Management and Service Fee | 83,998 | 88,986 |
| Gain (Loss) on Sale of Assets | 21,597,845 | (101,275) |
| Interest and Other Income | 663,157 | 812,653 |
| Total Non-Related Party Revenues | 53,543,608 | 33,803,517 |
| Related Party Revenues: | | |
| Management and Service Fee | 811,831 | 968,633 |
| Interest and Other Income | 220,950 | 210,453 |
| Total Related Party Revenues | 1,032,781 | 1,179,086 |
| Total Revenues | 54,576,389 | 34,982,603 |
| **EXPENSES** | | |
| Operating Expenses | 5,900,775 | 6,058,256 |
| Maintenance and Repairs | 3,983,977 | 4,296,228 |
| Depreciation and Amortization | 10,643,152 | 11,489,661 |
| Taxes Other than Income | 3,936,512 | 3,623,287 |
| General, Administrative and Other (Including Related Party) | 3,624,128 | 3,328,342 |
| Total Expenses before Interest and Income Taxes | 28,088,544 | 28,795,774 |
| **INTEREST EXPENSE** (Including Related Party) | 6,043,661 | 6,642,053 |
| Income (Loss) Before Provision (Benefit) for Income Taxes | 20,444,184 | (455,224) |
| **PROVISION (BENEFIT) FOR INCOME TAXES** | | |
| Current | (51,490) | (2,168) |
| Deferred | 7,881,612 | (239,101) |
| Total Provision (Benefit) for Income Taxes | 7,830,122 | (241,269) |
| **NET INCOME (LOSS)** | $ 12,614,062 | $ (213,955) |

See accompanying notes to the consolidated financial statements.

**TOWER PROPERTIES COMPANY & SUBSIDIARIES**
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**
**FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015**

| | 2016 | 2015 |
|---|---|---|
| **NET INCOME (LOSS)** | $ 12,614,062 | $ (213,955) |
| Unrealized holding gains on marketable equity securities, net of deferred tax expense of $1,738,666 and $107,306, respectively. | 2,719,450 | 167,838 |
| **COMPREHENSIVE INCOME (LOSS)** | $ 15,333,512 | $ (46,117) |

See accompanying notes to the consolidated financial statements.

**TOWER PROPERTIES COMPANY & SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF STOCKHOLDERS' INVESTMENT**

**FOR THE YEARS DECEMBER 31, 2016 AND 2015**

| | Common Stock | | | | Accumulated Other | Treasury Stock | | |
|---|---|---|---|---|---|---|---|---|
| | Shares | Amount | Paid-In Capital | Retained Earnings | Comprehensive Income | Shares | Amount | Total |
| Balance, December 31, 2014 | 6,181 | 6,181 | $ 19,108,978 | 18,969,350 | $ 5,675,593 | 1,395 | $ (11,736,817) | $ 32,023,285 |
| Net Loss | -- | -- | -- | (213,955) | -- | -- | -- | (213,955) |
| Unrealized Holding Gain for Securities net of deferred tax expense of $107,306 | -- | -- | -- | -- | 167,838 | -- | -- | 167,838 |
| Balance, December 31, 2015 | 6,181 | $ 6,181 | $ 19,108,978 | $ 18,755,395 | $ 5,843,431 | 1,395 | $ (11,736,817) | $ 31,977,168 |
| Net Income | -- | -- | -- | 12,614,062 | -- | -- | -- | 12,614,062 |
| Treasury Stock Purchases | -- | -- | -- | -- | -- | 585 | (7,018,000) | (7,018,000) |
| Unrealized Holding Gain for Securities net of deferred tax expense of $1,738,666 | -- | -- | -- | -- | 2,719,450 | -- | -- | 2,719,450 |
| Balance, December 31, 2016 | 6,181 | $ 6,181 | $ 19,108,978 | $ 31,369,457 | $ 8,562,881 | 1,980 | $ (18,754,817) | $ 40,292,680 |

See accompanying notes to the consolidated financial statements.

**TOWER PROPERTIES COMPANY & SUBSIDIARIES**

**CONSOLIDATED STATEMENTS OF CASH FLOWS**
**FOR THE YEARS ENDED DECEMBER 31, 2016 AND 2015**

| | 2016 | 2015 |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net Income (Loss) | $ 12,614,062 | $ (213,955) |
| Adjustments to Reconcile Net Income (Loss) to Net Cash Provided by Operating Activities: | | |
| Depreciation | 9,023,940 | 9,689,456 |
| Amortization | 1,619,212 | 1,800,195 |
| Amortization of Intangible Asset as Rent Income Reduction | 200 | -- |
| (Gain) Loss On Sale of Assets | (21,597,845) | 101,275 |
| Change in Balance Sheet Accounts, Net: | | |
| Receivables | 596,469 | 1,316,950 |
| Prepaid Expenses and Other Assets | (4,926) | (238,720) |
| Accounts Payable and Other Liabilities | 465,010 | 1,705,874 |
| Deferred Income Taxes | 7,881,612 | (239,101) |
| Current Income Taxes | (51,490) | (300,756) |
| Net Cash Provided by Operating Activities | 10,546,244 | 13,621,228 |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Proceeds from Disposition of Assets | 34,974,312 | -- |
| Acquisitions, net of cash acquired | (33,250,000) | -- |
| Purchases of Equipment and Furniture | (2,852,002) | (981,920) |
| Purchases of Rental Property | (17,552,575) | (7,681,117) |
| Purchases of Tenant Leasehold Improvements | (1,037,864) | (997,109) |
| Net Cash Used In Investing Activities | (19,718,129) | (9,660,146) |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Principal Payments on Mortgage Notes | (24,191,711) | (28,663,341) |
| Proceeds from Long Term Borrowings | 29,000,000 | 37,400,000 |
| Proceeds from Line of Credit Borrowings | 9,500,000 | -- |
| Payments on Line of Credit | (9,500,000) | (1,250,000) |
| Purchases of Treasury Stock | (7,018,000) | -- |
| Debt Issuance Costs | (183,559) | (279,751) |
| Net Cash Provided by (Used in) Financing Activities | (2,393,270) | 7,201,908 |
| NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS | (11,565,155) | 11,162,990 |
| CASH and CASH EQUIVALENTS, Beginning of Year | 13,205,980 | 2,042,990 |
| CASH and CASH EQUIVALENTS, End of Year | $ 1,640,825 | $ 13,205,980 |

See accompanying notes to the consolidated financial statements.

**TOWER PROPERTIES COMPANYAND SUBSIDIARIES**
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**
**DECEMBER 31, 2016 AND 2015**

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

### Business

Tower Properties Company and Subsidiaries (the Company) is primarily engaged in the business of owning, developing, leasing and managing real property located in Douglas and Johnson Counties in Kansas, and St. Louis County in Missouri. Substantially all of the improved real estate owned by the Company consists of office buildings, apartment complexes, a warehouse/office facility and land held for future sale or development.

### Principles of Consolidation

The accompanying consolidated financial statements include the accounts of Tower Properties Company and its majority owned subsidiaries. All significant intercompany balance and transactions have been eliminated in consolidation. The Company has no involvement with variable interest entities.

### Commercial Properties, Depreciation and Amortization

Commercial Properties are stated at cost less accumulated depreciation. Depreciation is charged to operations using straight-line and accelerated methods over the estimated asset lives, or in the case of tenant leasehold improvements, the term of the lease. The estimated useful lives of Commercial Properties range from 1 to 40 years with the majority of the assets having lives of 27.5 years or 39 years.

Maintenance and repairs are charged to expense as incurred. The cost of additions and betterments that improve or extend the useful life of the property are capitalized. Applicable interest charges incurred during the construction of new facilities are capitalized as one of the elements of cost and are amortized over the assets' estimated useful lives. The cost of assets retired or sold and the related accumulated depreciation are removed from the applicable accounts and any gain or loss is recognized as income or expense. Fully depreciated assets are retained in the accounts until retired or sold.

The amount of accumulated amortization on tenant leasehold improvements was $12,931,063 and $11,795,071 at December 31, 2016 and 2015, respectively.

The amount of accumulated depreciation on equipment and furniture was $18,666,637 and $22,432,838 at December 31, 2016 and 2015, respectively.

## Impairment of Long-Lived Assets

The Company assesses the carrying value of its long-lived assets whenever events or changes in circumstances indicate that the carrying amount of the underlying asset may not be recoverable. Certain factors that may occur and indicate that an impairment exists include, but are not limited to: significant underperformance relative to expected projected future operating results; significant changes in the manner of the use of the assets; and significant adverse industry or market economic trends. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeded its estimated future undiscounted cash flows, an impairment charge would be recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of are separately presented in the balance sheet as held for sale and reported at the lower of the carrying amount or fair value less costs to sell, and would no longer be depreciated.

## Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and short term investments with an original maturity of three months or less.

## Investment Securities

The Company classifies its investment securities as available-for-sale. Available-for-sale securities are recorded at fair value. Unrealized holding gains and losses, net of related tax effect, on available-for-sale securities are excluded from operations and are reported as a separate component of other comprehensive income until realized. A decline in the fair value of any security below cost that is deemed other than temporary would be charged to operations and result in the establishment of a new cost basis for the security.

## Revenue Recognition

The Company derives its revenue primarily from two sources: 1) rent from leases of real property, and 2) management and services fees from real property leased and managed. Rental revenue is recognized on a straight-line basis over the term of individual non-cancellable operating leases. The recognition of scheduled rent increases on a straight-line basis results in the recognition of a receivable from tenants. Such receivables were $876,541 and $962,427 at December 31, 2016 and 2015, respectively. Lease agreements generally do not provide for contingent rents. Amounts received from tenants upon early termination of leases are recorded when received as a reduction of lease receivables to the extent there is an associated straight line rent receivable, with the remainder recorded in other income. Management and service fees are recognized as a percentage of revenues on managed properties as earned over the terms of the related management agreements.

## Real Estate Held for Sale

The Company's real estate held for sale is recorded at the lower of depreciated cost or estimated realizable value. Revenue is recorded on the sale of real estate when title passes to the buyer and the earnings process is complete. Assets are generally classified as held for sale once management has

initiated an active program to market them for sale and has received a firm purchase commitment that is expected to close within one year. On occasion, the Company will receive unsolicited offers from third parties to buy individual Company properties. Under these circumstances, the Company will classify the properties as held for sale as of the date when a sales contract is executed with no contingencies and the prospective buyer has funds at risk to ensure performance.

**Consolidated Statements of Cash Flows**

Interest payments were $6,306,098 and $6,674,125 during the years ended December 31, 2016 and 2015, respectively. There were no income taxes paid during the year ended December 31, 2016. Income taxes paid, net of income tax refunds, amounted to $301,291 during the year ended December 31, 2015.

**Comprehensive Income (Loss)**

Comprehensive income (loss) includes charges and credits to equity that are not the result of transactions with shareholders. Comprehensive income (loss) is composed of two items-net income (loss) and other comprehensive income. Included in other comprehensive income are unrealized holding gains for investment securities.

**Recently Issued Accounting Standards**

In May, 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers. ASU 2014-09 requires an entity to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. An entity should also disclose sufficient quantitative and qualitative information to enable users of financial statements to understand the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers. The new standard is effective for annual reporting periods beginning after December 15, 2017. The Company will implement the provisions of ASU 2014-09 as of January 1, 2018. The Company has not yet determined the impact of the new standard on its current policies for revenue recognition.

In February, 2016, the FASB issued ASU 2016-02, Leases (Topic 842), which introduces a new model that requires most leases to be reported on the balance sheet and aligns many of the underlying principles of the new lessor model with those in the new revenue recognition standard. The standard requires the use of the modified retrospective (cumulative effect) transition approach. ASU 2016-02 is effective for the Company as of fiscal year 2019, with early adoption permitted. We are currently evaluating the effect that ASU 2016-02 will have on our consolidated financial statements and related disclosures, and we have not determined if we will early adopt.

In June 2016, the FASB issued ASU 2016-13, Financial Instruments-Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments, which provides new guidance regarding the measurement and recognition of credit impairment for certain financial assets. Such guidance will impact how we evaluate our available-for-sale investments for impairment. ASU 2016-13 is effective for the Company as of fiscal year 2020, with early adoption permitted. We are currently evaluating the

effect that ASU 2016-13 will have on our consolidated financial statements and related disclosures, and we have not determined if we will early adopt.

In January 2017, the FASB issued ASU 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business, which provides guidance regarding the definition of a business, with the objective of adding guidance to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. ASU 2017-01 is effective for the Company as of fiscal year 2018, with early adoption permitted, and prospective application required. We are currently evaluating the effect that ASU 2017-01 will have on our consolidated financial statements and related disclosures, and we have not determined if we will early adopt.

**Reclassifications**

Certain reclassifications have been made to the prior year amounts to conform to the current year presentation.

**Use of Estimates**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant items subject to such estimates and assumptions include the useful lives of fixed assets; allowances for doubtful accounts; valuation of deferred tax assets, acquired tangible and intangible assets and assumed liabilities in business combinations and investments; and reserve for income tax uncertainties and other contingencies.
The Company's accounting policies conform to accounting principles generally accepted in the United States of America.

## 2. RENTAL PROPERTY:

Major classes of rental property owned by the Company at December 31, 2016 and 2015, are as follows:

| | Cost | Accumulated Depreciation | Net |
|---|---|---|---|
| December 31, 2016— | | | |
| Commercial office | $109,499,846 | $ 22,372,037 | $ 87,127,809 |
| Apartments | 119,881,610 | 28,074,479 | 91,807,131 |
| Industrial | 3,932,005 | 2,033,413 | 1,898,592 |
| | $233,313,461 | $ 52,479,929 | $180,833,532 |

| | Cost | Accumulated Depreciation | Net |
|---|---|---|---|
| December 31, 2015— | | | |
| Commercial office | $ 66,379,118 | $ 20,683,463 | $ 45,695,655 |
| Apartments | 139,469,067 | 39,842,500 | 99,626,567 |
| Industrial | 3,932,005 | 1,952,973 | 1,979,032 |
| | $209,780,190 | $ 62,478,936 | $147,301,254 |

Future minimum rentals to be received by the Company, pursuant to noncancellable operating leases in effect as of December 31, 2017 are as follows:

| Year Ending December 31, | Amount |
|---|---|
| 2017 | $ 23,390,599 |
| 2018 | 11,688,199 |
| 2019 | 9,060,029 |
| 2020 | 5,733,196 |
| 2021 | 4,375,902 |
| Thereafter | 9,521,460 |
| | $ 63,769,385 |

## 3. LONG-TERM DEBT:

Mortgage notes payable secured by commercial property with depreciated cost of approximately $194,085,000 and $159,291,000 at December 31, 2016 and 2015, respectively and an assignment of certain leases and related revenue, consist of the following:

| | 2016 | 2015 |
|---|---|---|
| 5.89%, principal and interest payable | | |
| $35,505 monthly, until March, 2024 | $ 2,509,125 | $ 2,778,719 |
| 7.40%, principal and interest payable | | |
| $43,172 monthly, until April, 2016 | | |
| This note was paid in full in April, 2016 | - | 170,059 |
| 7.56%, principal and interest payable | | |
| $56,779 monthly, until April, 2021 | 2,510,602 | 2,982,598 |
| 5.56%, principal and interest payable | | |
| $74,121 monthly, until May, 2019 | | |
| final balloon payment due June, 2019 | | |
| This note was paid in full in June, 2016 | - | 8,432,171 |
| 5.18%, principal and interest payable | | |
| $53,561 monthly, until June, 2020 | | |
| final balloon payment due July, 2020 | 6,863,199 | 7,142,521 |
| 6.15%, principal and interest payable | | |
| $33,227 monthly, until September, 2017 | | |
| final balloon payment due October, 2017 | 1,950,269 | 2,219,986 |
| 6.39%, principal and interest payable | | |
| $25,397 monthly, until September, 2022 | | |
| final balloon payment due October, 2022 | 3,030,699 | 3,138,053 |
| 4.95%, principal and interest payable | | |
| $42,167 monthly, until August, 2018 | | |
| final balloon payment due September, 2018 | 5,712,045 | 5,924,728 |
| 5.04%, principal and interest payable | | |
| $106,775 monthly, until July, 2017 | | |
| final balloon payment due August, 2017 | 17,796,538 | 18,155,881 |
| 5.00%, principal and interest payable | | |
| $16,369 monthly, until June, 2021 | | |
| final balloon payment due July, 2021 | 2,449,822 | 2,521,789 |
| 5.00%, principal and interest payable | | |
| $9,353 monthly, until June, 2021 | | |
| final balloon payment due July, 2021 | 1,399,898 | 1,441,022 |

| | | |
|---|---|---|
| 5.00%, principal and interest payable | | |
| $47,790 monthly, until June, 2021 | | |
| final balloon payment due July, 2021 | 7,152,605 | 7,362,723 |
| 4.10%, principal and interest payable | | |
| $30,748 monthly, until September, 2021 | | |
| final balloon payment due October, 2021 | 4,991,141 | 5,148,479 |
| 4.75%, principal and interest payable | | |
| $45,507 monthly, until March, 2022 | | |
| final balloon payment due April, 2022 | 5,975,769 | 6,226,639 |
| 3.50%, principal and interest payable | | |
| $89,111 monthly, until November, 2022 | | |
| final balloon payment due December, 2022 | 15,886,646 | 16,390,345 |
| 3.31%, principal and interest payable | | |
| $72,060 monthly, until July, 2048 | 16,927,303 | 17,226,344 |
| 4.04%, principal and interest payable | | |
| $70,293 monthly, until May, 2025 | | |
| final balloon payment due May, 2025 | | |
| This note was paid in full in June, 2016 | - | 11,312,812 |
| 4.20%, principal and interest payable | | |
| $43,391 monthly, until July, 2025 | | |
| final balloon payment due July, 2025 | 6,696,280 | 6,925,681 |
| 4.00%, principal and interest payable | | |
| $100,374 monthly, until November, 2025 | | |
| final balloon payment due December, 2025 | 18,455,935 | 18,900,000 |
| 4.20%, principal and interest payable | | |
| $46,486 monthly, until August, 2025 | | |
| final balloon payment due September, 2025 | 7,460,336 | - |
| 3.50%, principal and interest payable | | |
| $57,996 monthly, until October, 2026 | | |
| final balloon payment due November, 2026 | 9,971,171 | - |
| 3.50%, principal and interest payable | | |
| $61,169 monthly, until October, 2026 | | |
| final balloon payment due November, 2026 | 10,469,456 | - |
| 3.75%, interest only payable until June 2018, | | |
| principal and interest payable $77,120 | | |
| monthly, July 2018 until November, 2026 | | |
| final balloon payment due December 2026 | | |
| not fully funded at December 31, 2016 | 1,000,000 | - |
| Total Mortgage Notes Payable | $ 149,208,839 | $ 144,400,550 |

Minimum long-term debt principal payments for mortgage notes required over the next five years and thereafter are as follows:

| Year | Amount |
|---|---|
| 2017 | $ 24,439,763 |
| 2018 | 10,180,935 |
| 2019 | 4,929,871 |
| 2020 | 10,749,224 |
| 2021 | 17,804,089 |
| Thereafter | 81,104,957 |
| | $ 149,208,839 |

The carrying amounts and estimated fair values of long-term debt are based on current market interest rates for similar issues as follows:

| 2016 | | 2015 | |
|---|---|---|---|
| Carrying Amount | Fair Value | Carrying Amount | Fair Value |
| $149,208,839 | $143,734,000 | $144,440,550 | $140,184,000 |

The fair values are based on the present value of future cash flows discounted at estimated borrowing rates for similar debt instruments or on estimated prices based on current yields for debt issues of similar quality and terms. The Company negotiates its long-term debt rates on a property by property basis. The carrying amount of the debt represents the actual face value of the contractual debt contracts. The fair value is an estimate of what the mortgage holder could resell the debt for at year end.

At December 31, 2016, the Company had no outstanding borrowings on the Line of Credit. For the period ended December 31, 2016, total payments on the Line of Credit amounted to $9,500,000 with total borrowings against the line of $9,500,000, with the maximum outstanding at any one time of $7,500,000. Payments on the Line of Credit for the year ended December 31, 2015 totaled $1,250,000.

On July 15, 2015, the Company financed a loan for the 7911 Forsyth Building. The loan is a $7,000,000 10-year non-recourse loan (20 year amortization) for 7911 Forsyth at 4.20% that matures with a balloon payment on July 15, 2025.

On September 1, 2015, the Company financed a loan associated with an 87 unit expansion of the Hutton Farms apartment complex. The loan is a $7,500,000 10-year loan (20 year amortization) at 4.20% that matures with a balloon payment on September 1, 2025. The Company constructed 87 apartment units as an expansion of the Hutton Farm complex in Lawrence, Kansas in 2016. This loan is both a construction loan that can be drawn down during the construction period, and a permanent loan after the full $7,500,000 was funded. At December 31, 2015 there was no funding from the Lender. All funding of the $7,500,000 loan was received on September 1, 2016. Initially, the $7,500,000 loan is a recourse loan. The loan will convert to a non-recourse loan after the occupancy of the apartments is normalized for six consecutive months.

On December 1, 2015, the Company refinanced the loan for the Hillsborough apartments. The original loan for Hillsborough had an outstanding balance of $13,994,993 at December 1, 2015. The Company paid off the existing loan for Hillsborough on December 1, 2015 and paid a prepayment penalty of $564,443 which is included in General, Administrative and Other Expense for the year ended December 31, 2015. The Company replaced the original loan on December 1, 2015 with a new $18,900,000, 10-year non-recourse loan (25 year amortization) for Hillsborough at 4.0%, that matures with a balloon payment on December 1, 2025.

On June 23, 2016, the Company paid off two loans associated with the New Mark apartments when New Mark was sold. A loan on Phases I, II, III, and IV of New Mark had an outstanding balance at the time of pay off of $11,121,746. The Company paid off the loan on June 23, 2016 and paid a prepayment penalty of $166,826 which is included in General, Administrative and Other Expense for the year ended December 31, 2016. A loan on Phase V of New Mark had an outstanding balance at the time of payoff of $8,219,407. The Company paid off the loan on June 23, 2016 and paid an a prepayment penalty of $1,027,248 which is included in General, Administrative and Other Expense for the year ended December 31, 2016.

On November 1, 2016, the Company financed a loan associated with the purchase of the Indian Creek Campus I office building at 10740 Nall. The new loan of $10,000,000 is a 10-year non-recourse loan (20 year amortization) at 3.5% that matures with a balloon payment on November 1, 2026.

On November 1, 2016, the Company financed a loan associated with the purchase of the Creekview Corporate Center office building at 12900 Foster. The new loan of $10,500,000 is a 10-year non-recourse loan (20 year amortization) at 3.5% that matures with a balloon payment on November 1, 2026.

On December 1, 2016, the Company financed a loan associated with the renovation of the 6601 College Boulevard Building. The loan is a $15,000,000 10-year loan (25 year amortization) at 3.75% that matures with a balloon payment on December 1, 2026. The loan requires interest only payments through June 1, 2018, and full debt service payments will begin on July 1, 2018. The Company is currently renovating the 6601 College Building and the base building renovation was completed in 2016 and the construction of tenant improvements is expected to be made in 2017 and 2018. This loan is both a construction loan that can be drawn down during the construction period, and a permanent loan after the full $15,000,000 is funded. The Company will draw down a total of $12,160,000 before June 1, 2017. At December 31, 2016, $1,000,000 was funded and outstanding, leaving $11,160,000 left to be borrowed before June 1, 2017 at the Company's request. Additional draws totaling $2,840,000 will be made as tenants lease space with the funding available at a maximum pace of 80% of tenant improvements and leasing commissions incurred by the Company and all $2,840,000 will be drawn down before June 1, 2018. All funding of the $15,000,000 loan will be completed by May 31, 2018. Initially, the $15,000,000 loan is a recourse loan. The loan will convert to a non-recourse loan after the occupancy of the building is normalized for three consecutive months.

## 4. INCOME TAXES:

The Company's effective income tax rate differed from the statutory federal income tax rate primarily due to the following:

| | 2016 | 2015 |
|---|---|---|
| Statutory federal income tax rate | 34.0% | (34.0)% |
| Tax effect of: | | |
| Dividend exclusion | (.3) | (11.2) |
| State income taxes, net of federal effect | 3.3 | (4.3) |
| Nondeductible travel & entertainment expense | 0.0 | 0.5 |
| Other | 1.3 | (4.0) |
| Effective income tax rate | 38.3% | (53.0)% |

Deferred income taxes are determined based on the difference between the financial statement and tax basis of assets and liabilities using the enacted tax rate. The tax effect of temporary differences giving rise to the Company's net deferred income tax liability at December 31, 2016 and 2015 is as follows:

| | 2016 | 2015 |
|---|---|---|
| Deferred tax assets: | | |
| Net Operating Loss | $ 1,785,000 | $ 1,585,000 |
| AMT Credit Carryforward | 523,057 | 523,057 |
| Amortization of leasehold improvements | 120,668 | 125,123 |
| Rent received in advance | 285,117 | 185,746 |
| Accrued vacation | 19,520 | 19,568 |
| Bad Debt | 23,690 | 38,384 |
| Gross deferred tax assets | 2,757,052 | 2,477,328 |
| Deferred tax liabilities: | | |
| Depreciation on rental income property, equipment and furniture | (18,657,250) | (10,378,388) |
| Unrealized holding gain for securities | (5,474,630) | (3,735,964) |
| Accrued rent receivable | (341,851) | (375,347) |
| Prepaid expenses | (262,248) | (346,278) |
| | (24,735,979) | (14,835,977) |
| Net deferred income tax liability | $ (21,978,927) | $ (12,358,649) |

Due to the history of earnings and projected future results, the Company believes it is more likely than not that future operations will generate sufficient taxable income to realize the deferred tax assets.

At December 31, 2016, the Company projects net operating loss carryforwards for federal income tax purposes of approximately $4,400,000 which are available to offset future federal taxable income, if any, through 2036. In addition, the Company has alternative minimum tax credit carryforwards of $523,057, which are available to reduce future federal regular income taxes, if any, over an indefinite period of time.

## 5. SALE AND ACQUISTIONS OF PROPERTIES:

On July 1, 2015, the Company purchased 14.415 acres of land in Lawrence, Kansas adjacent to the Company's Hutton Farms apartment complex. The purchase price was $800,000. The land was used for construction of a 45-building, 87-unit expansion of the Hutton Farms complex.

On June 23, 2016, the Company sold the New Mark apartments located in Kansas City, Missouri. The sales price was $35,000,000 which resulted in a net gain on sale of $21,621,527 and after the Company paid off the two associated loans, related interest expense and other reconciliations and costs at closing, $14,013,469 was paid in cash to an intermediary as the first step in a Sec. 1031 like-kind exchange.

On November 1, 2016, the Company purchased two office buildings in Overland Park, Kansas, Indian Creek Campus I at 10740 Nall and Creekview Corporate Center at 12900 Foster, for $33,250,000. The purchase of the two office buildings was the final step of a Sec. 1031 like-kind exchange. Of the $14,013,469 of cash held by the intermediary from the sale of the New Mark apartments, $1,225,000 was returned to the Company on November 1, 2016, with the remainder utilized in the purchase of the two office buildings.

Upon acquisition of real estate properties, the Company determines if the acquisition meets the criteria to be accounted for as a business combination in accordance with ASC 805. Acquisitions of properties with multiple tenants that require business related activities to manage and maintain the properties are treated as business combinations. Accordingly, the Company records the fair value of acquired tangible assets (consisting of land, buildings, tenant improvements, and furniture, fixtures and equipment) and identified intangible assets (consisting of acquired in-place leases and acquired above-market leases) and liabilities. The fair value of acquired in-place leases includes management's estimate of the value associated with avoiding the costs typically incurred during a lease-up period (i.e. the market cost to execute the leases, including leasing commissions, legal and other related operating costs). These values are amortized over the remaining initial lease term of the respective leases. The fair value of acquired above-market leases includes management's determination whether the terms of each operating lease is favorable or unfavorable compared with the market terms of similar leases at the acquisition date and an intangible asset is recorded if the terms of an operating lease are favorable relative to market terms. These values are amortized as a reduction of rent income over the remaining non-cancelable terms of the respective leases. Acquisition-related costs in connection with business combinations are expensed as incurred.

On the acquisition date of November 1, 2016, the Company recorded the following in the consolidated financial statements: $31,715,000 in tangible assets, comprising $5,650,000 of land, $1,846,600 of furniture and fixtures, and $24,218,400 of buildings and land improvements. The Company recorded an Intangible Asset-Acquired in Place Leases Value of $1,330,000, which will be amortized on a straight line basis over the approximate weighted average remaining lease terms (36 and 60 months). The Company recorded an Intangible Asset-Acquired Above Market Leases of $205,000, which will be amortized as a reduction of rent income over the remaining non-cancelable terms of the respective leases, with $200 in amortization recorded for the year ended December 31, 2016.

## 6. RELATED PARTY TRANSACTIONS:

An officer and some of the directors of the Company are also employees, officers and/or directors of Commerce Bank and Commerce Bancshares, Inc. and its subsidiaries ("Commerce"). Thomas R. Willard, President & CEO of the Company, also holds the position of Vice Chairman of the Commerce Trust Company, a division of Commerce Bank. In July, 2015, in an unanimous Consent of the Board of Directors ("BOD") of the Company, there was an acknowledgement that Thomas R. Willard, President and CEO of the Company, has also accepted the position of Vice Chairman of the Commerce Trust Company, a related party. To appropriately reflect Mr. Willard's reduced time commitment as President and CEO of the Company the BOD authorized and approved a reduction in his salary.

The Company earned management and service fees income from Commerce of $811,831 and $968,633 in 2016 and 2015, respectively.

The Company owns 257,759 shares of Commerce Bancshares, Inc. common stock, which is shown as a related party investment in the accompanying balance sheets. The common stock has a cost basis of $863,538. Total unrealized gains at December 31, 2016 and 2015 were $14,037,510 and $9,579,394 respectively. Dividend income received as owner of Commerce Bancshares, Inc. common stock was $220,950 and $210,453 in 2016 and 2015, respectively.

The Company's cash and cash equivalents are held at Commerce. There was no interest income earned from these cash and cash equivalents for the years 2016 and 2015.

The Company has a $13,500,000 line of credit ("Line of Credit") with Commerce Bank that carries a variable interest rate equal to one and three quarter percent (1 3/4 %) in excess of the one month maturity London Interbank Offered Rate ("LIBOR"). At December 31, 2016, the Company had no outstanding borrowings on the Line of Credit and if the Company had borrowings under the Line of Credit the interest rate would be 2.38%. The Line of Credit is collateralized by 257,759 shares of Commerce Bancshares, Inc. common stock and the warehouse/office facility at 9200 Cody. The warehouse/office facility at 9200 Cody was added as additional collateral for the Line of Credit on February 19, 2016. The Company had $13,500,000 available under the Line of Credit at December 31, 2016. This line requires monthly interest payments and matures June 1, 2017. The Company intends to renew the Line of Credit with Commerce upon maturity. Interest expense for the Line of Credit was $24,999 and $1,041 for 2016 and 2015, respectively. The weighted average short term borrowing rate for interest paid on the Line of Credit was 2.24% for the year ended December 31, 2016.

In 2012 the Company signed a new five-year lease renewal, which also includes a five-year renewal option, at their offices at 1000 Walnut, Suite 900, Kansas City, MO, a building owned by Commerce. Rent included in General, Administrative and Other expense was $72,191 and $68,793 for 2016 and 2015, respectively.

Included in receivables at December 31, 2016 and 2015 are amounts due from Commerce of $641,797 and $747,704, respectively.

## 7. BENEFIT PLANS:

Some of the Company's union employees are covered by union-sponsored, collectively-bargained, multi-employer pension plans. Tower contributed $86,308 and $78,048 in 2016 and 2015, respectively, to such plans. The contributions were determined in accordance with the provisions of negotiated labor contracts and are based on the number of hours worked. The Company has a 401(k) plan whereby the Company matches 25% of employee contributions up to a maximum Company match equal to 1.5% of employee compensation. The Company matched $36,228 and $37,882 for the years ended December 31, 2016 and 2015, respectively. The Company also made discretionary contributions in the amounts of $71,400 and $78,400 for the years ended December 31, 2016 and 2015, respectively.

## 8. STOCK BASED COMPENSATION:

In 2016 and 2015 the Company did not grant any stock options. There were no stock options outstanding at December 31, 2016 or 2015.

## 9. FAIR VALUE MEASUREMENTS:

US GAAP discusses valuation techniques, such as the market approach (prices and other relevant information generated by market conditions involving identical or comparable assets or liabilities), the income approach (techniques to convert future amounts to single present amounts based on market expectations including present value techniques and option-pricing), and the cost approach (amount that would be required to replace the service capacity of an asset which is often referred to as replacement cost). A fair value hierarchy that prioritizes the inputs to valuation techniques is used to measure fair value into three broad levels. The following is a brief description of those three levels:

Level 1: Observable inputs such as unadjusted quoted prices in active markets for identical assets or liabilities that the Company has the ability to access at the measurement date.

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets or liabilities in active markets and quoted prices for identical or similar assets or liabilities in markets that are not active.

Level 3: Unobservable inputs that reflect the reporting entity's own assumptions.

The Company uses fair value measurements to record fair value adjustments to certain financial and nonfinancial assets and liabilities and to determine fair value disclosures. Financial instruments such as investment securities are recorded at fair value on a recurring basis. Additionally, from time to time, the Company may be required to record at fair value other assets and liabilities on a nonrecurring basis, such as long-lived assets and intangible assets. These nonrecurring fair value adjustments typically involve lower of cost or market accounting, or write-downs of individual assets.

**Valuation methods for instruments measured at fair value on a recurring basis**

Investment securities are priced using the market prices for each security from the major stock exchanges or other electronic quotation systems.

The following tables show assets measured at fair value on a recurring basis and also the level within the fair value hierarchy used to measure the assets as of December 31, 2016 and 2015.

| | Balance December 31, 2016 | Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
|---|---|---|---|---|
| Assets: | | | | |
| Investment Securities | $ 14,901,048 | $ 14,901,048 | $ - | $ - |

| | Balance December 31, 2015 | Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
|---|---|---|---|---|
| Assets: | | | | |
| Investment Securities | $ 10,442,932 | $ 10,442,932 | $ - | $ - |

**Valuation methods for instruments measured at fair value on a nonrecurring basis**

While the long-lived assets are not carried at fair value, certain factors may occur that indicate an impairment exists. If an impairment charge would be recognized, it would be the amount by which the carrying amount of the asset exceeds the estimated fair value of the asset.

The Company initially measures its intangible assets at fair value, and amortizes them over the lease periods.

Fair value measurements may be based upon: a) appraisals or third-party price opinions and, accordingly, those measurements would be classified as Level 2, or b) internally developed pricing methods, and accordingly, those measurements would be classified as Level 3.

## 10. COMMITMENTS AND CONTINGENCIES:

At December 31, 2016, the Company has commitments to provide tenant improvement allowances in 2017 to five tenants that total $372,000.

From time to time, the Company is subject to various items related to the normal course of business, including loss of tenants, legal proceedings, and environmental related actions. In the opinion of management, none of these items are expected to result in a material adverse effect on the financial statements of the Company.

## 11. PURCHASES OF TREASURY STOCK

In 2016, the Company purchased a total of 585 shares of the Company's common stock at a total cost of $7,018,000, which are reflected as additions to Treasury Stock in the financial statements. The cash paid came out of the Cash and Cash Equivalents on hand.

On May 4, 2016, the Company purchased two shares of the Company's common stock owned by a non-related party shareholder for $11,000 per share for $22,000.

On May 16, 2016, the Company purchased all of the shares of the Company's common stock owned by Commerce as Trustee of Julianne Kemper, a related party of the Company. The Company purchased 583 shares at $12,000 per share for $6,996,000 which represented approximately 12% of the Company's then outstanding shares.

## 12. SUBSEQUENT EVENTS

The Company has evaluated subsequent events from the balance sheet date through March 31, 2017, the date at which financial statements were available to be issued, and determined there are no items to disclose.

## Independent Auditors' Report

The Board of Directors
Tower Properties Company and Subsidiaries:

**Report on the Financial Statements**

We have audited the accompanying consolidated financial statements of Tower Properties Company and its subsidiaries (the Company), which comprise the consolidated balance sheets as of December 31, 2016 and 2015, the related consolidated statements of operations, comprehensive income (loss), stockholders' investment and cash flows for each of the years in the two-year period ended December 31, 2016, and the related notes to the consolidated financial statements.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation 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 auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free 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 the auditors' 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, the auditor considers 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. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant 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 is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Tower Properties Company and its subsidiaries as of December 31, 2016 and 2015, and the results of their operations and their cash flows for each of the years in the two-year period ended December 31, 2016 in accordance with U.S. generally accepted accounting principles.

**/s/ KPMG LLP**

Kansas City, Missouri
March 31, 2017