

ANNUAL REPORT 2006



TABLE OF CONTENTS

Financial Highlights	02
President's Letter	03
Corporate Business	04
Management's Discussion and Analysis	07

FINANCIAL STATEMENTS

Management's Reporting Responsibility	15
Auditors' Report	15
Consolidated Balance Sheets	16
Consolidated Statements of Income	17
Consolidated Statements of Retained Earnings	18
Consolidated Statements of Cash Flows	19
Notes to Consolidated Financial Statements	20

LIST OF DIRECTORS

Hersh Spiegelman

Barry Dixon

Ruth Bartholomeusz

Bryan Ceresne

Daniel Kayfetz

Larry Cyna

CORPORATE PROFILE

Telehop Communications Inc. is a full-service long-distance provider operating within the telecommunications industry. Its main operations involve Wholesale services, Equal Access long distance services worldwide, Casual Calling services, Virtual Calling Card services, Toll Free services and Voice over Internet services.

CORPORATE DATA

Auditors

*Schwartz Levitsky Feldman LLP
1167 Caledonia Road, Toronto,
Ontario M6A 2X1*

Transfer Agents and Registrar

*Equity Transfer Services Inc.
120 Adelaide St. West, Suite 420
Toronto, Ontario M5H 4C3*

Bankers

*Bank of Nova Scotia
York Commercial Banking Centre
625 Cochrane Drive, Suite 200
Markham, Ontario L3R 9R9*

*HSBC Bank Canada
3640 Victoria Park Avenue
Willowdale, Ontario M2H 3B2*

Legal Counsel

*Stikeman, Graham, Keeley & Spiegel LLP.
220 Bay St. Suite 700
Toronto, Ontario M5J 2W4*

Share Listing/Ticker symbol

TSX Venture Exchange/HOP

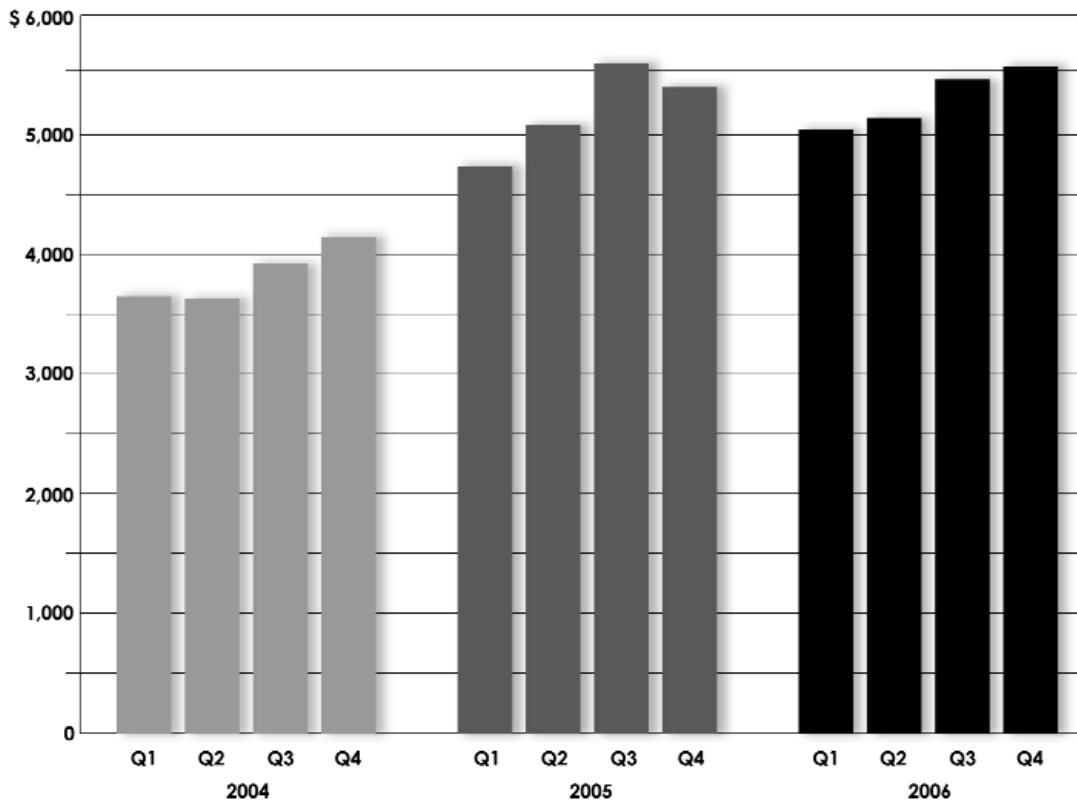
Head Office

*200 Consumers Road, Suite 220
Toronto, Ontario M2J 4R4
Telephone: (416) 494-4490
Fax: (416) 494-3788*

FINANCIAL HIGHLIGHTS

	Year ended December 31, 2006	Year ended December 31, 2005	Year ended December 31, 2004
Sales	\$ 21,181,302	\$ 20,770,191	\$ 15,325,613
Income before income taxes	1,565,733	978,147	550,106
Net income	1,024,182	611,065	284,983
Earnings per common share:			
Basic	\$ 0.08	\$ 0.05	\$ 0.02
Diluted	\$ 0.08	\$ 0.05	\$ 0.02
Total Assets	7,502,775	5,232,753	5,206,337
Shareholders' equity	4,225,725	3,231,587	2,605,621
Equity per common share	\$ 0.33	\$ 0.26	\$ 0.21

Quarterly Revenue Results
(000's of \$)



PRESIDENT'S LETTER

The year 2006 saw a tremendous focus on consolidation within Telehop Communications Inc. with its goal being to increase profitability and value to the shareholders. I am pleased to report success on both fronts. Your company ended the year in a very strong financial position, and paid its first ever dividend to its shareholders.

Telehop has been able to demonstrate its strength and stability through the delivery of profitable operational results for six consecutive years, along with significant growth in revenues, customer base, and traffic processed on the Telehop network. This was achieved in a period of significant market disruption by new technologies, and where barriers to entry in telecommunications have been reduced. The industry has seen long distance rates decline steadily for consumers over the past few years.

In 2006, Telehop spent significant development time and expense researching these new disruptive technologies, and is rolling out an expanded "Broadtalk™" Voice Over Internet Protocol ("VOIP") long distance service to the marketplace in 2007. Telehop still has ample spare capacity available on its existing switches and equipment to significantly increase its traffic throughput without major capital expenses.

Telehop continues to be able to internally finance its growth, and currently has significant free cash resources with no debt or capital leases on or off our balance sheet. This financial strength gives your Company the flexibility to pursue new opportunities as they arise.

We are continually working on expanding our market share by increasing our subscription base, which provides us with a more predictable and profitable revenue stream. This involves the development of marketing initiatives that we believe will assist us in gaining market share along with focusing on expanding our portfolio and adding services that we believe to be of value to our customers.

We could not have achieved these results without the hard work of our loyal and dedicated staff, and I would like to thank all our staff, customers and shareholders for their continued support that has enabled Telehop to position itself in the telecommunications industry as a significant and credible participant.

I will personally endeavor to ensure that your Company continues to pursue opportunities that I believe to be of value to all its stakeholders.

Sincerely,



Ruth Bartholomeusz,
President and Chief Operating Officer

May 8, 2007

CORPORATE BUSINESS

TELEHOP'S STRATEGY

Telehop Communications Inc.'s strategy is to attract and retain customers by offering significant savings over the telecom costs offered by the major competitors in the North American telecommunications market, whilst delivering quality service to its customers. Telehop maintains its profitability by identifying and catering to specific, targeted niche markets, and controls on its operating and administrative costs.

DESCRIPTION OF BUSINESS

Telehop is a full-service long distance provider operating within the telecommunications industry and is registered with the Canadian Radio-television and Telecommunications Commission ("CRTC") as a licensed Class "A" Telecom Carrier. Telehop currently employs 46 people.

Telehop's core network resides in Toronto, Ontario, with virtual points-of-presence in major cities across Canada.

The core network utilizes SS7 (signaling system 7) with circuit switched TDM (Time Division Multiplexing) connections and supports the latest in Voice Over Internet Protocol ("VOIP") technologies, including broadband telephony. The SS7 Signaling system allows Telehop to enhance service and feature delivery in terms of call quality and connection time to its end-users. In addition, network interconnections, voice-data convergence and interoperability with other carriers all depend on SS7. Telehop continues to strive to offer the highest quality of service to its customers by using the best telecommunications technology available.

Telehop has data systems in place for pre-emptive maintenance, ASR (Answer Seizure Ratio) reporting and online fraud management systems that serve as real-time quality control tools for calls made out of our switch and network health statistics.

Telehop's main service offerings include Wholesale Services, Equal Access long distance services worldwide, Casual Calling services, Virtual Calling Card services, "1-800" Toll Free services, BroadTalk service that allows customers to place calls to anywhere in the world from anywhere in the world using the BroadTalk gateway and a high-speed Internet connection and Directory Assistance services to its customer base through casual calling. This Directory Assistance service offers operator-assisted Directory Assistance through the use of 10-10-620. In 2006, telehop began offering 10-10-100 services to the west coast of Canada.

Telehop's Casual Calling services are extensively advertised in print and broadcast media in approximately 19 different languages, under the brand names "10-10-620" and "10-10-100". Telehop's extensive media coverage makes use of smart slogans that include "Talk More, Pay Less"; "Call the world for \$1" and "Hundreds of ways to save". Telehop's advertising campaign is based on the principal of "Speaking to the communities in their own language".

Telehop also offers "1+" direct access long distance across most cities in Canada that allows customers to dial long-distance without having to dial any prefixes other than the 1+ or 011+. Telehop is focusing on building its brand and has launched the 1+ service under the brand name WorldTalk. Telehop, as the parent brand, is promoting itself as the Smart Alternative.

Telehop is interconnected with major carriers in Canada, the United States, and other global carriers for domestic and international worldwide terminations. Telehop uses diverse carriers and routes for its traffic to ensure the highest level of redundancy and reliability.

CORPORATE BUSINESS

The range of long-distance services provided by Telehop Communications Inc. is outlined as follows:

"HOP" SERVICE

Telehop was one of the pioneers of unlimited long distance calling within an area covering most of the population base of Southern Ontario and Metropolitan Montreal.

Telehop wound down its HOP business at the end of 2006 due to changing market needs and the evolution of technology that made this particular service offering outdated.

"10-10-620" AND "10-10-100" CASUAL CALLING SERVICES

Telehop's Casual Calling services allow any user to access Telehop's long distance Equal Access network from most telephones across Canada, without having to subscribe to the service, or pay any monthly fees. The dial-around service or casual calling service allows a user to bypass or 'dial around' their existing long-distance provider on any call by entering the digits "10-10-620" or "10-10-100" before making a call, without having to switch carriers. Any calls made using Telehop's "10-10-620" and "10-10-100" Casual Calling services appear on the customers' regular, monthly local telephone bill at Telehop's discounted rates. Telehop has entered into Billing & Collection Agreements with a number of major Local Exchange Carriers ("LECs") across Canada.

EQUAL ACCESS SERVICE

Telehop's other major activity is providing "Equal Access" long distance services worldwide to its residential and business customers.

The term "Equal Access" refers to a long distance service that offers equal ease of access to all customers. This allows Telehop customers to directly dial long distance calls on Telehop's network using the normal '1+' or '011+' dialing pattern.

Telehop has been an Equal Access long distance provider since 1994.

WHOLESALE SERVICES

Telehop's Wholesale Service is based on trading bulk minutes worldwide with other similar carriers through its switching infrastructure. Wholesale customers use Telehop's network to carry their calls to any part of the world at discounted rates. Telehop's state-of-the-art gateways provide global connectivity to its switching centers that could be located anywhere in the world.

The incremental revenues generated by its wholesale sales channel provide the Company with more purchasing power when negotiating with other network providers and hence allows it to offer ultra competitive retail rates at a profit.

One of the main areas differentiating Telehop from its competition is the ability to provide its customers automated call detail data, including a complete billing service to its retail agents and wholesale resellers. The Company's strategy is not only to offer its end-users a broad array of products, but to also offer its key customers access to the Company's scalable automated infrastructure. Through its Wholesale Services website, the Company and its independent sales agents and resellers have almost real-time Internet access to billing records, instantaneous order entry and processing capabilities.

CORPORATE BUSINESS

VIRTUAL CALLING CARD SERVICE

The Telehop Virtual Calling Card is unique in that a customer does not need to acquire or purchase a physical card from a vendor or a convenience store. The user pre-pays the virtual card for a maximum dollar amount of long distance calling, and then the pre-paid Virtual Card can be easily replenished on the telephone or on the Internet. The Telehop Virtual Card account holders can also impose dollar limits and/or calling restrictions on their own cards. This is a useful tool for employers or families to control their long distance costs by setting predetermined spending limits on card users.

The user of a Telehop Virtual Calling Card can use this card from their home or office, or from any phone in North America, to call anywhere in the world at Telehop's standard discounted rates. The service is targeted at both corporate and residential sectors and is offered as a value-added service to our customers.

TOLL FREE SERVICE

Telehop is a reseller of Toll Free services. The Toll Free numbers 1-800, 1-855, 1-877 & 1-866 are offered to customers and billed at Telehop's discounted rates based on usage.

Telehop also offers its customers a worldwide, outbound toll free number, which allows them the ability to terminate a North American Toll Free number on any telephone in any country in the world.

BROADTALK SERVICE

Telehop is a reseller of Voice over Internet Protocol service, branded as BroadTalk. This service allows any customer that has access to a high-speed Internet connection to place calls to anywhere in the world from anywhere in the world using the BroadTalk gateway and a regular phone. The service is targeted at both corporate and residential sectors and is offered as a value-added service to our customers with very competitive calling rates.

DIRECTORY ASSISTANCE SERVICE

Telehop is a reseller of Directory Assistance service through casual calling. This service offers operator-assisted directory assistance to users that dial 00-10-620-0. The charges appear on the customer's regular monthly phone bill at discounted rates that are 50% below normal directory assistance rates.

MANAGEMENT'S DISCUSSION AND ANALYSIS

For the year ended December 31, 2006

Dated April 13, 2006

Management's Discussion and Analysis ("MD&A") is intended to help shareholders, analysts and other readers understand the dynamics of Telehop Communications Inc.'s ("Telehop") business and the key factors underlying its financial results. It explains trends in Telehop's financial condition and operating results for the year ended December 31, 2006 compared with the operating results for the year ended December 31, 2005. The MD&A should be read in conjunction with the Audited Consolidated Financial Statements for the year-ended December 31, 2006.

FORWARD-LOOKING STATEMENTS

The consolidated financial statements and information and analysis in the management's discussion and analysis necessarily includes amounts and conclusions based on informed judgments and estimates of the expected effects of current events and transactions with appropriate consideration as to materiality. In addition, in preparing the financial information, management must interpret the requirements described above, make determinations as to the relevancy of information to be included, and make estimates and assumptions that affect reported information.

Certain statements in the MD&A also constitute forward-looking statements. Such forward-looking statements involve known and unknown risks, uncertainties, and other factors that may cause the results, performance or achievements of Telehop to be materially different from those expressed or implied by such statements. Such factors include, amongst others, the following: general economic and business conditions, demographic changes, regulation, major technology changes, timing of product introductions, competition, and the ability of Telehop to attract and retain key employees.

This MD&A is comprised of two sections:

OVERALL PERFORMANCE

OUTLOOK

MANAGEMENT'S DISCUSSION AND ANALYSIS

OVERALL PERFORMANCE

Despite an increasingly challenging environment, Telehop managed to increase its customer base through the acquisition of equal access customers. Telehop increased its number of 'direct dial' subscription customers by 43% resulting in a 'direct dial' call revenue increase of 50% from 2005. Revenue per minute declined during 2006 from 6 cents in 2005 to 5 cents in 2006. This caused casual calling revenues to decline by 2%. A positive trend, however, is the general decline in telecom costs that has contributed greatly to our gross margins. Particularly, the issuance of a retroactive rate adjustment by the CRTC in 2006 helped increase Telehop's gross margins.

Telehop continues to focus on its core strengths in successfully targeting to specific niche markets. We've also managed to maintain a low cost structure, as the company continues to look for ways to increase efficiency. We are also very fortunate and grateful to the skillful and experienced employees at Telehop who have made significant contributions to the company year-over-year. This dynamic teamwork has allowed us to react swiftly to market changes. Telehop continues to see the declining revenue per minute as a challenge to growth; however, we will concentrate our efforts in building value to our customers and providing attractive packages that will help us increase revenue per customer.

The competitive landscape in 2006 continues to be challenging as new technologies and downward pressure on selling prices require each telecom competitor to constantly evaluate their markets, product mixes and cost structures to maintain their market share. Despite a 12.5% decline in revenue per minute, the company was able to maintain its revenues by increasing minutes by 15.5% and number of calls by 40.8%. Gross margins greatly improved in 2006 due to efficiency gains in fixed telecom costs and from rate adjustments mandated by the CRTC.

Key developments for Telehop's 2006 year were:

- A significant increase in long-distance traffic of 40.8% in the total number of calls carried and 15.5% in the total number of minutes over 2005 traffic.
- Increase in profitability by 67.6% to \$1,024,182 from \$611,065 in 2005
- Increase in gross margins to 44.5% from 41.8%, or \$9.4 million from \$8.7 million contributed from declining fixed telecom costs, retroactive rate credit adjustment credits mandated by CRTC, and the increase in subscription-based revenues
- Increase in overall retail revenues by 6%, driven mainly by a 50% increase in subscription-based revenues.
- Maintaining operating costs as a percentage of sales at 35% for 2006 and 2005.
- The successful launch of the new per-minute casual calling service, "10-10-100", in western Canada in early 2006.

RESULTS OF OPERATIONS

For the year ended December 31, 2006 the overall financial and operating condition of the Company improved with a modest increase in retail revenues despite an increasingly price-competitive market, and reduction in telecom costs that greatly contributed to gross margin improvements.

The key factors were:

- Gross margin improvement to 44.5% from 41.8% contributed by declining fixed telecom costs (0.7%), retroactive rate adjustments for variable telecom costs mandated by the CRTC (1.1%), and a 2% net increase in overall revenues (0.9%)
- Decrease in wholesale revenues by 13.4% which was intended to eliminate unprofitable resellers.
- Increase in subscriptions revenues by 50%, contributing to overall increase in retail revenues by 6%

MANAGEMENT'S DISCUSSION AND ANALYSIS

- Increase in EBITDA by \$597,794 or 42.7%
- Increase in working capital by 48% or \$1.0 million through increase in profits and better cashflow management (working capital ratio maintained at 2.1 for 2006 and 2005)

All these factors are described in detail below.

The per-minute rates for long distance traffic declined by 12.5% in 2006 over 2005. However, we also saw a parallel decline in telecom costs as fixed telecom costs decreased by 7% and variable telecom costs decreased by 43%, due to the retroactive rate adjustments mandated by the CRTC, as well as effective monitoring and control through negotiations with our telecom suppliers.

In 2006, Telehop continued to focus on the managing of its revenue streams to optimize profitability. Telehop was successful in increasing its total traffic minutes by 15.5% or 50.4 million minutes over 2005, ending the year with a total of 376.6 million minutes. The total number of calls also increased significantly with 26.5 million more calls than in 2005, which translated to a 40.8% increase over the previous year, for a total of 91.5 million calls in 2006 versus 64.5 million calls in 2005. Telehop saw a decrease in revenues per minute from 6 cents per minute in 2005 to 5 cents per minute in 2006., which is in line with the trends in the overall market.

REVENUE

Total revenues increased modestly in 2006 by 2.0% over 2005 with an increase of \$0.4 million. Although total revenues remained relatively flat, the product mix change between retail versus wholesale made a positive impact on gross margins.

CARRIER CHARGES AND OPERATING COSTS

(\$ thousands)

	2006	%	2005	%
Revenue	21,181	100.0	20,770	100.0
Telecom costs	11,749	55.0	12,082	58.2
Gross profit	9,432	44.5	8,688	41.8
Operating costs	7,434	35.1	7,288	35.1
EBITDA *	1,998	9.4	1,400	6.7
Depreciation	421		419	
Interest	12		3	
Taxes	541		367	
Net Income	1024		611	
EPS	\$ 0.08		\$ 0.05	
Diluted EPS	\$ 0.08		\$ 0.05	

* Earnings before Interest, Taxes, Depreciation and Amortization. EBITDA is a measure that has no standardized meaning prescribed by Canadian GAAP and is considered a non-GAAP measure. Therefore, the measure may not be comparable to similar measures presented by other issuers. This measure is described and presented in the MD&A, in order to provide shareholders and potential investors with additional information regarding the Company's liquidity and ability to generate funds to finance its operations.

MANAGEMENT'S DISCUSSION AND ANALYSIS

TELECOM COSTS

In spite of a 16% increase in minutes and a 41% increase in the total number of calls carried, Telehop's total telecom costs as a percentage of revenue declined by 2.7% from 2005. This was due to a 0.8% decline in fixed telecom costs as a percentage of revenue and the 1.6% decrease in variable telecom costs which was largely driven by the rate adjustment mandated by the CRTC (1.1% contribution). Rate adjustments have been common occurrences in the past few years as the CRTC is attempting to ensure fair competition among all Local Exchange Carriers by having Incumbent Local Exchange Carriers charge more equitable rates in their telecom services.

Fixed telecom costs decreased by 7% as a percentage of revenue in 2006 over 2005. This is attributed to a decline in fixed rates.

Telehop's proprietary 'Telehop Management System' software provides management with real-time information which enables more intelligent call routing and costing, allowing management detailed information by destination.

OPERATING COSTS

General & administration costs remained relatively flat with a slight decline of \$43,310, or 1.4%, from 2005. As a percentage of sales, the company managed to maintain these costs at 15% year-over-year.

Marketing and selling expenses decreased in 2006 by \$58,478, or 0.6% as a percentage of revenue, from \$3.5 million in 2005 to \$3.4 million in 2006. The decrease in marketing and selling costs was mainly attributed to higher costs incurred for launch of the casual calling service, "10-10-100", in Ontario in early 2005.

Development and technical support increased by \$247,991 or 1.0% as a percentage of revenue at 4.0% in 2006 and 3.0% 2005. This increase was mainly driven by increase in the hiring of key support and development staff, as well as increase in wages, to ensure the company's technical resources are retained and devoted to researching new applications and technologies.

FINANCIAL SUMMARY

	2006	2005	2004	2003	2002
Total revenue	21,181,302	20,770,191	15,325,613	15,587,884	12,334,438
Income	1,565,733	978,147	550,106	1,477,153	178,654
Net income	1,024,182	611,065	284,983	930,672	95,792
Net income per share	0.08	0.05	0.02	0.08	0.01
Diluted net income per share	0.08	0.05	0.02	0.08	0.01
Total assets	7,502,775	5,232,753	5,195,255	5,138,923	4,105,485
Total liabilities	3,208,000	2,001,166	2,589,634	2,953,446	2,859,332
Shareholders' equity	4,225,725	3,231,587	2,605,621	2,185,477	1,246,153
Return on equity	27%	21%	12%	54%	8%
Book value per share	\$ 0.33	\$ 0.26	\$ 0.21	\$ 0.18	\$ 0.10

MANAGEMENT'S DISCUSSION AND ANALYSIS

SUMMARY OF QUARTERLY RESULTS

	2005					2006				
	Q1	Q2	Q3	Q4	Total	Q1	Q2	Q3	Q4	Total
	(\$ thousands)									
Revenue	4,729	5,072	5,581	5,388	20,770	5,037	5,130	5,452	5,562	21,181
EBITDA*	284	108	257	751	1,400	530	449	556	463	1,998
Income	173	4	150	651	978	407	363	449	347	1,566
Net income	110	3	96	402	611	263	221	287	253	1,024
Earnings per share										
Basic	0.01	0.00	0.01	0.03	0.05	0.02	0.02	0.02	0.02	0.08
Diluted	0.01	0.00	0.01	0.03	0.05	0.02	0.02	0.02	0.02	0.08

* Earnings before Interest, Taxes, Depreciation and Amortization. EBITDA is a measure that has no standardized meaning prescribed by Canadian GAAP and is considered a non-GAAP measure. Therefore, the measure may not be comparable to similar measures presented by other issuers. This measure is described and presented in the MD&A, in order to provide shareholders and potential investors with additional information regarding the Company's liquidity and ability to generate funds to finance its operations.

LIQUIDITY

At the present time Telehop has sufficient cash on hand, and anticipates that it will continue to generate sufficient cash from its normal, ongoing business to fund any working capital and/or normal course capital expenditures for the foreseeable future.

Total operating lease commitments are as follows:

2007	184,185
2008	184,185
2009	184,185
2010	184,185
2011	157,616
	894,356

The Company continues to operate under its infrastructure lease, which includes premises and facilities.

The company's cash position at year end was \$2,778,664 and continues to maintain a strong working capital ratio of 2.0.

The company's contractual obligations as at December 31, 2006 were as follows:

Long-term debt	Nil
Capital lease obligations due within one year	Nil
Operating lease obligation due within one year	184,185
Purchase obligation	Nil
Other long-term obligations	Nil
	184,185

MANAGEMENT'S DISCUSSION AND ANALYSIS

CASH FLOW

In 2006, the Company generated cash from operating activities of \$2,313,737 up from cash generated from operating activities of \$55,037 in 2005.

The significant increase in cash from operations was attributed to several factors. In 2005, the conversion of our accounting system required us to reduce our accounts payable earlier than expected by approximately \$0.9 million at the end of December, 2005. This event did not re-occur in 2006 as the management of working capital improved significantly with an increase of \$0.8 million. In addition to improved working capital management, the increase in net income by \$0.4 million was also a key contributing factor.

The Company has adequate working capital to fund 2007 operations and foresees no requirement for outside financing at this point in time. Working capital at the end of 2006 totalled \$3.1 million, a 47% improvement of \$1.0 million from the working capital of \$2.1 million in 2005.

The Company has sufficient cash resources to finance future foreseeable capacity expansions. Management views the keys to expanding traffic as being continued targeted marketing and careful and selective expense management.

Book value of property, plant and equipment and intangible assets decreased slightly by \$13,804 after applying depreciation and amortization of \$420,548 for the year. Cash used in investing activities totalling \$406,745 included the purchase of communication equipment, enhancements to our in-house database management system, and acquisition of licenses of softphones.

The Company also raised \$53,300 from the issuance of common shares from the exercising of stock options by various employees during the year.

CAPITAL RESOURCES

The company has no commitments to any capital expenditures as the company's main source of financing is from cash from operations.

OFF-BALANCE SHEET ARRANGEMENTS

The company has no off balance sheet arrangements.

TRANSACTIONS WITH RELATED PARTIES

There were no transactions with related parties during the year.

CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with Canadian generally accepted accounting principles 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. The valuation of the allowance for doubtful accounts is managed on a monthly basis where provisions are applied at various percentages for accounts receivable categorized by risk.

MANAGEMENT'S DISCUSSION AND ANALYSIS

PENSION PLAN

The Company offers defined benefit pension plans to its executive employees. The pension plan expense for defined benefits plans is determined using the projected method pro-rated on years of service. The pension plan expense includes:

- Cost of pension plan benefits provided in exchange for employees' service rendered during the period;
- Amortization of prior service costs and amendments on a straight line basis over the expected average remaining service life of the employees covered by the plan; and
- Interest cost of pension plan obligations, the expected return on pension fund assets, and the amortization of cumulative unrecognized net actuarial gains and losses in excess of 10% of the greater of the projected benefit obligation of fair value of plan assets over the expected average remaining service life of the employee group covered by the plans.

The Company values pension plan assets at fair value, which is determined using current market value rates. Net benefit cost recognized in 2006 was \$65,967 (2005 - \$70,990).

FOURTH QUARTER 2006

Telehop's revenue for the three months ended December 31, 2006 was \$5,562,250, an increase of \$173,923 or 3%, compared to \$5,388,327 for the same period in 2005. Net income in the 2006 fourth quarter was \$253,762 (\$0.02 per share) compared to \$402,109 (\$0.03 per share) in 2005, a decrease of \$148,347 or 36.9%. The decrease was mainly due to higher marketing costs incurred in the quarter by \$174,721 which was mostly attributed to the launch of our "free directory assistance" marketing campaign. The revenues for this launch is expected to be realized in 2007.

Telehop's total long distance traffic processed by the Company for Q4 in 2006 showed significant growth over the comparable quarter in 2005. The total long distance traffic for Q4 in 2006 increased to 107.7 million minutes in 25.0 million calls, versus a total of 86.7 million minutes in 18.5 million calls in the same quarter of 2005. This was attributed to the increase in wholesale and subscriptions traffic over 2005.

Telehop's total telecom costs increased to \$3.1 million in Q4 of 2006 from \$2.9 million in Q4 of 2005. This represented an increase of 5% as a percentage of revenues over the comparative quarter, which was the result of a general rate reduction for retail markets and traffic mix.

General & administration costs for Q4 in 2006 decreased by \$61,001 compared to Q4 of 2005. This decrease was mainly due to lower professional and management consultant fees.

Marketing and selling costs for Q4 in 2006 was \$996,544, a \$174,721 increase over Q4 of 2005. The increase was attributed to the launch of "free directory assistance" service as described previously which increased marketing expenses as a percentage of revenue to 17.9% from 15.0% in Q4 of 2005.

CAPITALIZATION

As of April 13, 2007 the Company had 12,803,500 common shares outstanding and 1,015,000 common share purchase options, which are exercisable at prices ranging between \$0.20 and \$0.37 per share at varying times before June 24, 2010.

MANAGEMENT'S DISCUSSION AND ANALYSIS

RISK RELATED BUSINESS

You should carefully consider the following risk factors as well as the information included in this Report together with our consolidated financial statements and the related notes in evaluating our business and prospects.

The increase in range of services offered by our competitors could adversely impact our business. Telecommunications providers are continually increasing the range of services they offer. This trend may lead to a greater ability among our competitors to provide a comprehensive range of telecommunications services, which could lead to a reduction in demand for our services. Moreover, new services introduced by competitors could reduce the number of our current or potential customers.

Our business is dependent upon our ability to keep pace with the latest technological changes. The market for our services is characterized by rapid change and technological improvements. Failure to respond in a timely and cost-effective way to these technological developments could result in serious harm to our business and operating results. We have derived, and we expect to continue to derive, a substantial portion of our revenues from providing telecommunications services that are based upon today's leading technologies and that are capable of adapting to future technologies. Our success will depend, in part, on our ability to afford the cost of acquiring new hardware and software associated with new technologies, develop and market service offerings that have significant customer demand, respond in a timely manner to the technological advances of our customers, evolving industry standards and changing client preferences.

Other factors include:

- long distance telecommunications market and the economic conditions generally.
- fluctuations in demand for our services.
- reductions in the prices of services offered by our competitors.
- costs of integrating technologies or businesses that we add.
- the timing of expansion into new markets, both domestically and internationally.

OUTLOOK

Delivering the highest quality of service to each of our customers is paramount to Telehop's long-term sustainability. In 2007, Telehop will focus on new service offerings and markets to drive both revenue growth and profitability while improving on the overall customer experience and satisfaction.

This goal can be achieved through the following:

- Revenue growth:
 - Researching customers' needs and finding new markets to launch new services that will provide a sustainable competitive advantage and a solid revenue stream.
 - Finding new and creative marketing ideas to maintain and drive revenue growth.
- Productivity gains:
 - Maintaining tight controls on overhead costs.
 - Optimization of our network through improved monitoring.
 - Improvement in product mixes to increase gross margins.
 - Consolidation of our marketing channels to lower marketing costs.

In summary, Telehop sees a challenging road ahead in face of increasing competition in its core business. However, changing trends in the telecom industry has opened new doors as customer needs are ever-changing and Telehop can quickly address those needs. The company intends on capitalizing on these opportunities as it will explore opportunities in domestic as well as international markets in the upcoming year.

MANAGEMENT'S REPORTING RESPONSIBILITY

The accompanying consolidated financial statements of Telehop Communications Inc. and its subsidiaries are the responsibility of management and have been approved by the Board of Directors.

Management in conformity with Canadian generally accepted accounting principles has prepared the financial statements. The financial statements include some amounts that are based on best estimates and judgments. Financial information used elsewhere in the annual report is consistent with that in the financial statements.

Management of the Company and its subsidiaries, in furtherance of the integrity and objectivity of data in the financial statements, has developed and maintains a system of internal accounting controls. Management believes that this system of internal accounting controls provides reasonable assurance that, financial records are reliable and form a proper basis for preparation of financial statements and, that assets are properly accounted for and safeguarded.

The Board of Directors carries out its responsibility for the financial statements in this annual report principally through its audit committee. The audit committee reviews the Company's annual consolidated financial statements and recommends their approval to the Board of Directors. The shareholders' auditors have full access to the audit committee, with and without management being present.

These financial statements have been examined by the shareholders' auditors, Schwartz Levitsky Feldman LLP., and their report is presented below.



Ruth Bartholomeusz
President & COO



John Ng
Chief financial Officer

AUDITOR'S REPORT

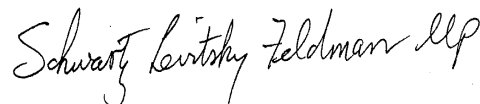
To the Shareholders of
Telehop Communications Inc.

We have audited the consolidated balance sheets of Telehop Communications Inc. as at December 31, 2006 and 2005 and the consolidated statements of income, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2006 and 2005 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Toronto, Ontario
March 20, 2007



Chartered Accountants
Licensed Public Accountants

CONSOLIDATED BALANCE SHEET

December 31, 2006 and 2005

2006

2005

ASSETS

CURRENT

Cash and cash equivalents	\$ 2,778,664	\$ 832,735
Accounts receivable (net of allowance for doubtful accounts of \$13,899; \$62,247 in 2005)	3,319,359	3,156,492
Prepaid expenses and deposits	236,881	61,851
	6,334,904	4,051,078
PROPERTY, PLANT AND EQUIPMENT (Note 4)	809,543	854,430
INTANGIBLES (Note 5)	358,328	327,245
	\$ 7,502,775	\$ 5,232,753

LIABILITIES

CURRENT

Accounts payable and accrued liabilities	\$ 3,020,690	\$ 1,884,722
Income taxes payable	187,310	32,874
Obligations under capital lease (Note 6)	-	14,363
	3,208,000	1,931,959
FUTURE INCOME TAX LIABILITY (Note 3)	69,050	69,207
	3,277,050	2,001,166

SHAREHOLDERS' EQUITY

CAPITAL STOCK (Note 7)	1,277,968	1,200,419
CONTRIBUTED SURPLUS (Note 7(b))	174,261	154,819
RETAINED EARNINGS	2,773,496	1,876,349
	4,225,725	3,231,587
	\$ 7,502,775	\$ 5,232,753

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

APPROVED BY THE BOARD



Barry Dixon
Director



Bryan Ceresne
Director

CONSOLIDATED STATEMENTS OF INCOME

Years ended December 31, 2006 and 2005	2006	2005
REVENUE	\$ 21,181,302	\$ 20,770,191
EXPENSES		
Telecom costs	11,749,483	12,082,369
General and administration	3,110,327	3,153,637
Marketing and selling	3,478,640	3,537,118
Development and technical support	844,844	596,853
Amortization expense	420,548	419,522
Interest expense	11,727	2,545
	19,615,569	19,792,044
INCOME BEFORE INCOME TAXES	1,565,733	978,147
INCOME TAX EXPENSE (Note 3)	541,551	367,082
NET INCOME FOR THE YEAR	\$ 1,024,182	\$ 611,065
EARNINGS PER SHARE (Note 9)	\$ 0.08	\$ 0.05
DILUTED EARNINGS PER SHARE (Note 9)	\$ 0.08	\$ 0.05

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS

Years ended December 31, 2006 and 2005	2006	2005
Balance at beginning of year as previously reported	\$ 1,876,349	\$ 1,265,284
Income for the year	1,024,182	611,065
Dividend declared	(127,035)	-
Balance end of year	\$ 2,773,496	\$ 1,876,349

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended December 31, 2006 and 2005	2006	2005
CASH FLOW PROVIDED BY (USED FOR)		
OPERATING ACTIVITIES		
Net income for the year	\$ 1,024,182	\$ 611,065
Adjustments for non-cash items:		
Amortization expense	420,548	419,522
Future income tax liability	(157)	(7,836)
Stock compensation (Note 7(b))	43,692	14,901
	1,488,265	1,037,652
Changes in working capital items :		
Accounts receivable	(162,867)	(614,983)
Prepaid expenses and deposits	(175,030)	42,814
Accounts payable and accrued liabilities	1,008,933	(598,560)
Income taxes payable	154,436	188,114
Cash provided by operating activities	2,313,737	55,037
INVESTING ACTIVITIES		
Acquisitions of property, plant and equipment	(353,081)	(469,847)
Acquisition of intangibles	(53,664)	-
Cash used for investing activities	(406,745)	(469,847)
FINANCING ACTIVITY		
Capital lease financing	(14,363)	(14,946)
Issuance of common shares	53,300	-
Cash provided by (used for) financing activities	38,937	(14,946)
Net increase (Decrease) in cash position	1,945,929	(429,756)
CASH POSITION, BEGINNING OF YEAR	832,735	1,262,491
CASH POSITION, END OF YEAR	\$ 2,778,664	\$ 832,735

SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION

Non-cash Financing Activities

Dividend declared	\$ 127,035	\$ -
Contributed surplus allocated to share capital on exercise of employee stock options during year	\$ 24,250	\$ -

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. NATURE OF BUSINESS

Telehop Communications Inc. is a full-service long distance provider operating within the telecommunications industry and is registered with the Canadian Radio-television and Telecommunications Commission ("CRTC") as a licensed Class 'A' Telecom Carrier.

2. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and reflect the following policies:

Basis of consolidation

The consolidated financial statements include the accounts of the Company and its subsidiaries, all of which are wholly owned. All intercompany transactions and accounts have been eliminated on consolidation. Subsidiaries are as follows:

Telehop Communications Inc.

International Telehop Network Systems Inc.

Telehop Long Distance Services Limited.

Telehop Long Distance Limited.

Card Tel Corp.

Telehop Agencies Inc.

Telehop Global Israel Inc.

Telehop Carrier Services Inc.

Telehop Premium Business Services Inc.

Telehop Rebillers Limited.

Ten-Ten-Six-Twenty Ltd.

The Friend Network Inc.

The Friend Network Services Inc.

Worldhop. Com.Inc.

Measurement uncertainty

The preparation of financial statements in conformity with Canadian generally accepted accounting principles 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. The valuation of the allowance for doubtful accounts, recoverability of intangible assets, and specific telecom accruals are the key areas where management employs the use of estimates and assumptions. Given the use of estimates inherent in the financial reporting process, actual results could differ from those estimates.

Cash and cash equivalents

For purposes of the consolidated financial statements, cash and cash equivalents is defined as cash and short-term deposits having a maturity of three months or less.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Property, plant and equipment

When events or changes in circumstances indicate the carrying amount of a long-lived asset may not be recoverable, an impairment loss is recognized when the carrying amount of those assets exceeds the sum of the undiscounted future cash flows related to them. The impairment loss is included in the statement of income (loss) and the carrying value of the asset is reduced to its fair value as determined by the sum of the discounted future cash flows related to those assets.

Property, plant and equipment are recorded at cost and are amortized based on the estimated useful lives of the assets using the straight-line method over the following periods:

Telecom equipment	- 5 years
Automobile	- 5 years
Furniture and equipment	- 5 years
Computer Equipment	- 2 years
Leasehold improvements	- 5 years
Telecom switch	- 7 years
Computer software	- 5 years

Intangible assets

Intangible assets are comprised of the following items: a system for telephone call data management and billing, a system for enhanced accounting and financial reporting, and software licenses for 3,000 softphones. All intangible assets are amortized over their estimated useful life on a straightline basis over 5 years. Management reviews the intangible assets for amortization and useful life annually and also for impairment whenever events or changes in circumstances indicate that full recoverability is questionable. Management measures any potential impairment by comparing the carrying value to the undiscounted amounts of expected future cash flows.

Translation of foreign currencies

Monetary assets and liabilities denominated in foreign currencies are translated at exchange rates in effect at the balance sheet dates. Revenues and expenses are translated at exchange rates prevailing during the period. Translation gains and losses are reflected in net income and have been disclosed in Note 10.

Post-employment benefits

The cost of providing benefits through defined benefit pensions is actuarially determined and recognized in earnings using the projected benefits method pro-rated on service. Differences arising from plan amendments, changes in assumptions and experience gains and losses are recognized in earnings over the expected average remaining service life of employees. The cost of providing benefits through defined contribution pension plans is charged to earnings when contributions become payable.

Actuarial gains and losses that fall outside a corridor defined as the greater of (a) 10% of the accrued benefit obligation and (b) 10% of the fair market value of the plan assets at the beginning of the year are amortized over the average remaining service period of active employees on a straight-line basis. The expected return on plan assets is based on the fair value of plan assets.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Income taxes

The Company uses the asset and liability method for accounting for income taxes which requires the establishment of future tax assets and liabilities, as measured by substantively enacted tax rates, for all temporary differences caused when tax bases of assets and liabilities differ from those reported in the financial statements. Future tax assets are recognized only to the extent that, in the opinion of management, it is more likely than not that the future income tax assets will be realized. Future tax assets and liabilities are adjusted for the effects of changes in tax laws and rates on the date of substantive enactment.

Revenue recognition

The Company records revenue from retail and wholesale services at the time of customer usage primarily based upon minutes of use. The Company recognizes revenues on the accrual basis and includes an estimate of revenues earned but not billed. Revenue is only recognized where there is reasonable assurance of collection. Royalty revenue is received monthly in arrears and accrued in the applicable month it is earned.

The Company makes a provision for bad debts using management's best estimate. The provision is netted against accounts receivable. The provision is reviewed on a regular basis by management.

Stock option plan and change in accounting policy

The Company has an employee stock option plan, which is described in Note 7.

The Company accounts for stock-based compensation in accordance with the CICA Handbook Section 3870, "Stock-based Compensation & Other Stock-based Payments". Section 3870 requires that all stock-based awards made to employees and non-employees be measured and recognized using a fair value based method, such as the Black-Scholes option pricing model. Previously the standard encouraged the use of a fair value based method for all awards granted to employees but only required the use of a fair value based method for direct awards of stock, stock appreciation rights, and awards that call for settlement in cash or other assets.

Refer to Note 7(a) for additional disclosure on stock-based compensation.

Earnings per share

The Company uses the treasury stock method of calculating the dilutive effect of options on earnings per share, whereby any proceeds obtained upon exercise of options is assumed to be used to purchase common shares at the average market share price during the period, except in the instance where such a calculation would be anti-dilutive.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Guarantees

In 2003 the Company adopted the new recommendations of the Canadian Institute of Chartered Accountants' Accounting Guideline 14, "Disclosure of Guarantees". In the normal course of business, the Company has guaranteed a portion of the residual values of certain assets under operating leases with expiry dates between June 2004 and November 2006, for the benefit of the lessor, the carrying value of which are \$NIL (2005 \$NIL). If the Company elects not to purchase or release the assets at the end of their respective lease term, then the Company must, under certain conditions, compensate the lessor for a portion of any shortfall between the fair value and the residual value. The maximum exposure in respect of these guarantees is approximately \$5,000.

3. INCOME TAXES

INCOME TAX EXPENSE

The income tax expense for the years ended December 31, is as follows:

	2006	2005
Current	\$ 541,708	\$ 374,918
Future	(157)	(7,836)
	\$ 541,551	\$ 367,082

FUTURE INCOME TAX ASSETS AND LIABILITIES

Future income tax assets and liabilities as at December 31, 2006 and 2005 were as follows:

	2006	2005
Future income tax liability		
Accounting base of property, plant and equipment in excess of tax value	\$ 69,050	\$ 69,207
Long-term	\$ 69,050	\$ 69,207

RECONCILIATION OF PROVISIONS TO STATUTORY RATES

The reconciliation of income taxes at Canadian statutory rates to the provision for income taxes is as follows:

	2006	2005
Income before income taxes	\$ 1,565,733	\$ 978,147
Approximate applicable statutory tax rate	36.12%	36.12%
Income taxes at statutory tax rates	565,543	353,307
Adjustment to prior year's provision		
Non-deductible amounts	2,552	7,757
Other	(26,544)	6,018
	\$ 541,551	\$ 367,082

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

4. PROPERTY, PLANT AND EQUIPMENT

	2006			2005		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Telecom equipment	\$ 1,411,966	\$ 832,583	\$ 579,383	\$ 1,222,463	\$ 619,192	\$ 603,271
Telecom switch	938,139	938,139	-	938,139	938,139	-
Computer software	284,756	120,853	163,903	253,892	72,947	180,945
Computer equipment	1,544	386	1,158	-	-	-
Leasehold improvements	190,539	152,408	38,131	162,698	124,936	37,762
Furniture and equipment	100,694	76,948	23,746	91,969	65,317	26,652
Automobile	12,889	9,667	3,222	12,889	7,089	5,800
	\$ 2,940,527	\$ 2,130,984	\$ 809,543	\$ 2,682,050	\$ 1,827,620	\$ 854,430

Amortization expense for the year-end December 31, 2006 is \$303,363 (2005: \$311,541).

5. INTANGIBLES

	2006			2005		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Internally Developed Software	\$ 634,633	\$ 329,075	\$ 305,558	\$ 540,029	\$ 212,784	\$ 327,245
Software Licenses	\$ 53,664	\$ 894	\$ 52,770	\$ -	\$ -	\$ -
	\$ 688,297	\$ 329,969	\$ 358,328	\$ 540,029	\$ 212,784	\$ 327,245

Amortization expense for the year end December 31, 2006 is \$117,185 (2005: \$107,981).

6. OBLIGATIONS UNDER CAPITAL LEASE

The Company had entered into leases in prior years for certain equipment that have been capitalized. No capital leases exist as at December 31, 2006.

	2006	2005
2006	-	14,929
Total minimum lease payments	-	14,929
Less amount representing imputed interest of approximately 6%	-	566
Present value of obligations under capital lease	-	14,363
Current portion - due within one year	-	14,363
Long-term obligations under capital lease	\$ -	\$ -

Interest expense for the year end December 31, 2006 is \$867 (2005 \$2,545)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

7. SHAREHOLDERS' EQUITY

Authorized

An unlimited number of common shares

Issued and outstanding

The changes in common shares for 2006 and 2005 are as follows:

	2006		2005	
	No. of Shares	Amount	No. of Shares	Amount
Balance, beginning of year	12,437,000	\$ 1,200,419	12,437,000	\$ 1,200,419
Issued on exercise of employee stock options (Note 7(a))	266,500	77,549	-	-
Balance, end of year	12,703,500	\$ 1,277,968	12,437,000	\$ 1,200,419

(A) STOCK OPTIONS

The Company's employee stock option plan ("ESOP") authorized the Company to reserve 1,800,000 common shares of the Company for issuance in accordance with the terms of the ESOP. Options granted vest over a period not exceeding five years and the purchase price is payable in full at the time the options are exercised.

The following table presents information concerning stock options granted under the Company's stock option plan:

	2006		2005	
	Number of options	Weighted Average Exercise Price	Number of options	Weighted Average Exercise Price
Options outstanding, beginning of year	1,289,500	\$ 0.24	1,089,500	\$ 0.24
Options granted	100,000	0.37	200,000	0.34
Options exercised	(266,500)	0.20		
Options cancelled	(8,000)	0.20		
Options outstanding, end of year	1,115,000	\$ 0.26	1,289,500	\$ 0.26
Options exercisable, end of year	1,085,000	\$ 0.25	1,164,500	\$ 0.25

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

7. SHAREHOLDERS' EQUITY (continued)

(A) STOCK OPTIONS (CONTINUED)

The following table summarizes information about stock options outstanding at December 31, 2006:

Weighted Average Exercise Price	Options Outstanding		Options Exercisable	
	Number Outstanding	Weighted Average Remaining Contractual Life	Number Exercisable	Weighted Average Exercise Price
\$ 0.20	510,000	1.05 years	510,000	\$ 0.20
\$ 0.30	100,000	3.46 years	100,000	\$ 0.30
\$ 0.32	5,000	2.94 years	5,000	\$ 0.32
\$ 0.35	300,000	1.72 years	300,000	\$ 0.35
\$ 0.37	200,000	3.90 years	170,000	\$ 0.37
	1,115,000	1.27 years	1,085,000	\$ 0.28

All options were below market value at the time of granting.

The Company has evaluated the fair value of all options granted during the past four years using the Black-Scholes option pricing model with the noted assumptions:

	December 31, 2006	December 31, 2005
	Weighted Average	Weighted Average
Estimated fair value at the date of grant for options granted in the period	\$0.30 - \$0.50	\$0.18 - \$0.19
Assumptions utilized:		
Risk-free interest rate	3.90%	3.29%
Expected volatility	72%	79%
Expected life of the options	5 years	5 years
Dividend Yield	0%	0%

(B) CONTRIBUTED SURPLUS

The following is a continuity of the changes in contributed surplus for the year ended December 31, 2006:

	2006	2005
Balance at beginning of year	\$ 154,819	\$ 139,918
Stock-based compensation expense during the year	43,692	14,901
Allocated to share capital on exercise of options during the year	(24,250)	-
Balance at end of year	\$ 174,261	\$ 154,819

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

8. EMPLOYEE BENEFIT PLANS

The changes in the benefit obligations and in the fair value of assets and the funded status of the benefit plans are as follows:

	Registered Pension Plans	
	2006	2005
Change in benefit obligations		
Projected benefit obligation, beginning of year	\$ 308,414	\$ 243,875
Current service cost	47,921	44,577
Interest cost	27,147	19,962
Actuarial (gains) losses	(29,582)	-
Benefit payments	-	-
Employee contributions	-	-
Prior service costs	-	-
Benefit obligation, end of year	353,900	308,414
Change in fair value of plan assets		
Fair value of plan assets, beginning of year	161,592	-
Return on plan assets	19,682	6,102
Benefit payments	-	-
Employer contributions	55,894	105,912
Employee contributions	-	49,578
Fair value of plan assets, end of year	237,168	161,592
Funded status (plan deficit)	(116,732)	(146,822)
Unamortized net actuarial (gain) loss	-	-
Unamortized past service costs	150,628	163,181
Unamortized transitional (asset) obligation	(27,610)	-
Valuation allowance	-	-
Accrued benefit asset (liability)	6,286	16,359

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

8. EMPLOYEE BENEFIT PLANS (continued)

The table below shows the net benefit plan cost before and after recognizing its long-term nature. The recognized net benefit plan cost reflects the amount reported in the Company's statement of income and is calculated according to the Company's accounting policy.

	Registered Pension Plans	
	2006	2005
Current service cost	\$ 47,921	\$ 44,577
Interest cost	27,147	19,962
Actual return on assets	(19,682)	(6,102)
Actuarial loss on accrued benefit obligation	-	-
Elements of employee future benefit plans cost, before recognizing its long-term nature	55,386	58,437
Actuarial loss	-	-
Difference between the actual return and estimated return on plan assets	-	-
Amortization of transitional asset (obligation)	-	-
Amortization of past service cost	12,553	12,553
Amortization of net actuarial loss	(1,972)	-
Others	-	-
Adjustment to recognize long-term nature of employee future benefit plans credit	10,581	12,553
Increase in valuation allowance	-	-
Net benefit plans cost recognized	\$ 65,967	\$ 70,990

The significant actuarial assumptions adopted in measuring the Company's accrued benefit obligations are as follows:

	2006	2005
Discount rate	7.5%	7.5%
Expected long-term rate of return on plan assets	7.5%	7.5%
Rate of compensation increase	5.5%	5.5%

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

9. EARNINGS PER SHARE

The Company uses the treasury stock method of calculating the dilutive effect of options on earnings per share. The following table sets forth the computation of basic and diluted earnings per share:

	2006	2005
Net Income	\$ 1,024,182	\$ 611,065
Weighted-average shares for earnings per share	12,508,844	12,437,000
Effect of dilutive securities - Employee stock options	310,040	242,887
Adjusted weighted-average shares and assumed conversions for diluted earnings per share	12,818,884	12,679,887
Earnings per share	\$ 0.08	\$ 0.05
Diluted earnings per share	\$ 0.08	\$ 0.05

10. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

CREDIT RISK

The Company is subject to credit risk through accounts receivables, which is limited by the large number of customers and their geographic dispersion across Ontario. The Company has credit evaluation, approval and monitoring processes intended to mitigate potential credit risks, and maintains provisions for potential credit losses that are assessed on an ongoing basis.

More than 50% of the Company's receivables are owed by a few Competitive Local Exchange Carriers (CLEC's) across Canada. These CLEC's provide billing and collection services to the Company's customers through an arrangement whereby the Company is limited to a fixed percentage exposure. In mitigation the Company purchases long distance services from these carriers for similar amounts owed at any time.

The Company is dependent in Ontario, Quebec, British Columbia, Alberta, Saskatoon and Manitoba upon carriers to provide billing and collection services to its customers under renewable agreements. Management expects that these agreements will automatically renew.

The Company purchases long distance services from a number of carriers and does not feel there is any economic dependence on any one carrier

FAIR VALUE OF FINANCIAL INSTRUMENTS

The carrying amounts of financial instruments included in current assets and current liabilities approximate their estimated fair values at December 31, 2006 and 2005, reflecting the short-term maturity and normal trade credit terms of these instruments. The carrying value of the Company's long-term obligation associated with the capital lease approximates fair value of the instrument, given prevailing interest rates for such arrangements.

FOREIGN EXCHANGE RISK

Foreign exchange risk arose because of fluctuations in exchange rates. The Company conducts a portion of its business activities in the United States. The assets, liabilities, revenues and expenses denominated in United States dollars will be affected by changes in the exchange rate between the Canadian dollar and the United States dollar.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

10. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (continued)

The net foreign exchange loss for 2006 was \$14,932 (2005 \$13,248) and has been recorded in the general and administration expense.

FOREIGN EXCHANGE CONTRACTS

The company enters into forward foreign exchange contracts ("Forwards") to mitigate its foreign currency exposure on expenses incurred for its operations. The forwards obligate the Company to buy US dollars with Canadian dollars in the future at predetermined exchange rates and are matched with anticipated future operating expenses that are transacted in US dollars.

As at December 31, 2006, the company had \$1,000,000 in US dollar forwards, with no maturity dates, at an average exchange rate of 1.134. An unrealized foreign exchange gain of \$31,495 exists as at December 31, 2006.

11. COMMITMENTS

OPERATING LEASES

The future minimum payments under operating leases as at December 31, 2006 are as follows:

2007	184,185
2008	184,185
2009	184,185
2010	184,185
Thereafter	157,616
	<hr/>
	\$ 894,356

12. SEGMENTED INFORMATION

The Company has determined that it has one reportable segment. The Company's operations are substantially all related to the provision of telecommunication services to the residential and business sectors. All assets of the business support these operations and are located in Canada.

13. SUBSEQUENT EVENTS

Between January and February of 2007, 100,000 shares were issued from the exercise of stock options by a former director. The issuance of shares raised total proceeds of \$20,000.

14. CONTINGENT LIABILITY

The Company is in negotiations with a former executive involving a dispute that pertains to the terms of a settlement with the company dating back to 2004. One of the terms of the settlement is being disputed as to whether it has been fully satisfied by the Company. The Company is pursuing to bring closure to this settlement with the former executive. The outcome cannot be determined at this time and no provision has been recorded.

15. COMPARATIVE FIGURES

Certain of the comparative figures have been reclassified to conform to the current period's presentation.

PERSONAL NOTES

A series of horizontal dotted lines for writing notes, filling the majority of the page.

PERSONAL NOTES

A series of horizontal dotted lines for writing notes, filling the majority of the page.

PERSONAL NOTES

A series of horizontal dotted lines for writing notes.

PERSONAL NOTES

A series of horizontal dotted lines for writing notes.

PERSONAL NOTES

A series of horizontal dotted lines for writing notes.

PERSONAL NOTES

A series of horizontal dotted lines for writing notes.

200 Consumers Road, Suite 220
Toronto, Ontario M2J 4R4
Telephone: (416) 494 4490
Fax: (416) 494 3788
www.telehop.com

