

Consolidated Financial Statements of

TELEHOP COMMUNICATIONS INC.

December 31, 2007 and 2006

Schwartz Levitsky Feldman llp

CHARTERED ACCOUNTANTS
LICENSED PUBLIC ACCOUNTANTS
TORONTO • MONTREAL



AUDITORS' REPORT

To the Shareholders of
Telehop Communications Inc.

We have audited the consolidated balance sheets of Telehop Communications Inc. as at December 31, 2007 and 2006 and the consolidated statements of income and comprehensive income, retained earnings and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform the 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, 2007 and 2006 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

A handwritten signature in cursive script that reads "Schwartz Levitsky Feldman llp".

Toronto, Ontario
April 1, 2008

Chartered Accountants
Licensed Public Accountants

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TELEHOP COMMUNICATIONS INC.

Consolidated Balance Sheets

As at December 31, 2007 and 2006

	2007	2006
ASSETS		
CURRENT		
Cash and cash equivalents (Note 4)	\$ 2,882,305	\$ 2,778,664
Accounts receivable (net of allowance for doubtful accounts of \$74,648; \$13,899 in 2006)	2,875,202	3,319,359
Income taxes recoverable	291,495	-
Prepaid expenses and deposits	88,246	236,881
	6,137,248	6,334,904
PROPERTY AND EQUIPMENT (Note 6)	769,346	809,543
INTANGIBLE ASSETS (Note 7)	267,454	358,328
	\$ 7,174,048	\$ 7,502,775
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities	\$ 2,565,416	\$ 2,893,655
Dividend payable	267,270	127,035
Income taxes payable	-	187,310
Obligations under capital lease (Note 8)	15,253	-
	2,847,939	3,208,000
FUTURE INCOME TAXES (Note 5)	32,284	69,050
OBLIGATIONS UNDER CAPITAL LEASE (Note 8)	47,185	-
	2,927,408	3,277,050
SHAREHOLDERS' EQUITY		
SHARE CAPITAL (Note 9)	1,527,177	1,277,968
CONTRIBUTED SURPLUS (Note 9(b))	40,489	174,261
RETAINED EARNINGS	2,678,974	2,773,496
	4,246,640	4,225,725
	\$ 7,174,048	\$ 7,502,775

Commitments (Note 13)

Related Party Transactions (Note 14)

Contingent Liability (Note 16)

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

APPROVED BY THE BOARD

"Hersh Spiegelman"

..... Chairman of the Board

"Maurice Cohen"

..... Director

TELEHOP COMMUNICATIONS INC.
Consolidated Statements of Income and Comprehensive Income
Years ended December 31, 2007 and 2006

	2007	2006
OPERATING REVENUES	\$ 17,983,269	\$ 21,055,434
Telecommunications costs	10,554,593	11,749,483
GROSS MARGIN	7,428,676	9,305,951
OPERATING EXPENSES		
General and administration	3,220,896	3,110,327
Marketing and selling	2,580,811	3,478,640
Development and technical support	952,495	844,844
Amortization	461,798	420,548
Interest	29,221	11,727
	7,245,221	7,866,086
OPERATING INCOME	183,455	1,439,865
Other income	165,077	125,868
INCOME BEFORE INCOME TAXES	348,532	1,565,733
Income taxes (Note 5)	175,784	541,551
NET INCOME	172,748	1,024,182
Other comprehensive income	-	-
COMPREHENSIVE INCOME	\$ 172,748	\$ 1,024,182
EARNINGS PER SHARE (Note 11)	\$ 0.01	\$ 0.08
DILUTED EARNINGS PER SHARE (Note 11)	\$ 0.01	\$ 0.08

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

TELEHOP COMMUNICATIONS INC.
Consolidated Statements of Retained Earnings
Years ended December 31, 2007 and 2006

	2007	2006
Retained earnings, beginning of year	\$ 2,773,496	\$ 1,876,349
Net income for the year	172,748	1,024,182
Dividend declared	(267,270)	(127,035)
Retained earnings, end of year	\$ 2,678,974	\$ 2,773,496

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

TELEHOP COMMUNICATIONS INC.

Consolidated Statements of Cash Flows

Years ended December 31, 2007 and 2006

	2007	2006
CASH FLOW PROVIDED BY (USED FOR)		
OPERATING ACTIVITIES		
Net income for the year	\$ 172,748	\$ 1,024,182
Adjustments for non-cash items:		
Amortization expense	461,798	420,548
Future income tax liability	(36,766)	(157)
Stock-based compensation	(49,063)	43,692
	548,717	1,488,265
Changes in working capital items:		
Accounts receivable	444,157	(162,867)
Prepaid expenses and deposits	148,635	(175,030)
Accounts payable and accrued liabilities	(328,239)	1,008,933
Income taxes recoverable/payable	(478,805)	154,436
Cash provided by operating activities	334,465	2,313,737
INVESTING ACTIVITIES		
Acquisitions of property and equipment	(211,987)	(353,081)
Acquisition of intangible assets	(52,635)	(53,664)
Cash used for investing activities	(264,622)	(406,745)
FINANCING ACTIVITIES		
Obligations under capital lease	(3,667)	(14,363)
Dividend paid	(127,035)	-
Issuance of common shares	164,500	53,300
Cash provided by financing activities	33,798	38,937
NET INCREASE IN CASH POSITION	103,641	1,945,929
CASH POSITION, BEGINNING OF YEAR	2,778,664	832,735
CASH POSITION, END OF YEAR	\$ 2,882,305	\$ 2,778,664

SUPPLEMENTARY DISCLOSURE OF CASHFLOW INFORMATION

Non-cash Financing Activities

Dividends payable	\$ 267,270	\$ 127,035
Contributed surplus allocated to share capital on exercise of employee stock options during the year	\$ 84,709	\$ 24,250
Obligations under capital lease	\$ 62,438	\$ -

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

TELEHOP COMMUNICATIONS INC.

Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

1. NATURE OF BUSINESS

Telehop Communications Inc. (the Company) 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 (GAAP) 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, of which the principal company is Telehop Communications Inc. All intercompany transactions and accounts have been eliminated on consolidation.

Use of 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. Given the use of estimates inherent in the financial reporting process, actual results could differ from those estimates. Examples of significant estimates include:

- Allowance for doubtful accounts
- Estimated useful lives of assets
- Recoverability of intangible and tangible assets
- The amount of income tax assets and liabilities
- Certain actuarial and economic assumptions used in defining defined benefit pension costs, accrued pension obligations and pension plan assets

Cash and cash equivalents

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

Impairment of long-lived assets

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 consolidated statements of income and comprehensive income 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. For the year ended December 31, 2007, there were no impairment losses recognized in the consolidated statements of income and comprehensive income.

TELEHOP COMMUNICATIONS INC.
Notes to the Consolidated Financial Statements
December 31, 2007 and 2006

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Property and equipment

Property 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	- 3 years
Leasehold improvements	- 5 years
Telecom switch equipment	- 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 soft phones. All intangible assets are amortized over their estimated useful life on a straight-line 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 date with any resulting gain or loss being included in the consolidated statements of income and comprehensive income. Trade transactions are translated at exchange rates prevailing during the period.

Employee future 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. 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.

TELEHOP COMMUNICATIONS INC.
Notes to the Consolidated Financial Statements
December 31, 2007 and 2006

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 earns its revenues from access to, and usage of, its telecommunications network. Its main service is to provide long-distance services through the access of our network, which has the capability to track pertinent data for each individual call to a particular country destination. This allows the Company to rate each call by applying pre-determined long-distance rates by country to the volume of minutes provided. 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 persuasive evidence of an arrangement exists, services have been rendered and a price to the customer is fixed or determinable. There were no revenue arrangements with multiple deliverables during the year. The Company mainly sells one type of service which is packaged in different forms which includes casual calling, subscriptions and wholesale.

Casual Calling

This service allows customers to access the Company's network without the need to subscribe to the service, sign a contract or pay any direct fees. Customers can complete a long-distance call by dialing one of two carrier identification codes (CIC), "10-10-100" or "10-10-620", that are owned by the Company. Revenue is recognized when a customer dials our CIC's and completes a connected long-distance call.

Subscriptions

Equal access service- This service allows a customer to directly dial their long distance number, by dialing "1+" or "011+". The customer subscribes to this service and is required to transfer carriers upon sign up. Revenue is recognized when a customer completes a long-distance call as access and usage of the Company's network has occurred.

TELEHOP COMMUNICATIONS INC.
Notes to the Consolidated Financial Statements
December 31, 2007 and 2006

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

High-speed internet – The Company resells high-speed internet services on subscriptions basis. Revenue is recognized when internet service has been provided.

Broadtalk – The Company resells a VOIP (voice-over-internet-protocol) service under its Broadtalk brand. This service allows a customer to place local and long-distance calls through a high-speed internet connection; thus, allowing the customer to replace their home phone. Revenue is recognized when the customer is billed each month for usage of the VOIP box and for long-distance calls placed.

Virtual Calling Card - The Company offers a virtual calling card such 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 prepaid balance is recorded as deferred revenue and revenue is recognized as the customer places long-distance calls.

Wholesale

The Company offers discounted rates to high volume users who typically want to carry their calls through the Company's network. Bulk minutes are sold by destination to these users who frequently repackage them with their own unique services which are then sold to their customers. Revenue is recognized when the reseller's customers make long-distance calls through the access and usage of the Company's network.

Telecommunications costs

Telecommunications costs primarily include fixed and variable carrier costs, billing and collections charges from Local Exchange Carriers (LECs) and operating lease expenses related to telecommunications equipment facilities.

Stock-based compensation

The Company has an employee share option plan, which is described in Note 9. Canadian GAAP requires that all share-based awards made to employees and non-employees be measured and recognized in the financial statements using a fair value based method, such as the Black-Scholes option pricing model. Proceeds arising from the exercise of share options are credited to share capital.

When stock-based compensation vests in fixed amounts at a future point in time, the expense is recognized by the Company in the Consolidated Statements of Income and Other Comprehensive Income on a straight-line basis over the vesting period.

Refer to Note 9 (a) for additional disclosure on stock-based compensation.

TELEHOP COMMUNICATIONS INC.

Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

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.

Leases

Leases are classified as capital or operating depending upon the terms and conditions of the contracts. Asset values recorded under capital leases are amortized on a straight-line basis over the period of expected use. Obligations recorded under capital leases are reduced by lease payments net of imputed interest.

3. CHANGES AND DEVELOPMENTS IN ACCOUNTING POLICIES

Changes in Accounting Policies

Effective January 1, 2007, the Company adopted five new accounting standards that were issued by the Canadian Institute of Chartered Accountants (“CICA”): *Comprehensive Income* (“Section 1530”), *Hedges* (“Section 3865”), *Financial Instruments – Recognition and Measurement* (“Section 3855”), *Equity* (“Section 3251”), and *Financial Instruments – Disclosure and Presentation* (“Section 3861”). These new Handbook Sections, which apply to fiscal years beginning on or after October 1, 2006, provide comprehensive requirements for the recognition and measurement of financial instruments, as well as standards on when and how hedge accounting may be applied. These accounting policy changes were adopted on a prospective basis with no restatement of prior period financial statements.

Comprehensive Income

Section 1530 requires the presentation of comprehensive income, which consists of net income and other comprehensive income (“OCI”). Comprehensive income is defined as the change in equity from transactions and other events from non-owner sources. OCI refers to items recognized in comprehensive income but that are excluded from net income calculated in accordance with generally accepted accounting principles. A new financial statement has been presented in relation to the new standards.

Financial Instruments – Recognition and Measurement and Disclosure and Presentation

Section 3855 establishes standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives. All financial assets and financial liabilities, including derivatives, are measured in the balance sheet at fair value, except for loans and receivables, investments held-to-maturity and other financial liabilities, which are measured at amortized cost. Measurement in subsequent periods depends on whether the financial instrument had been classified as held-for-trading, available-for-sale, held-to-maturity, loans and receivables, or other liabilities.

TELEHOP COMMUNICATIONS INC.
Notes to the Consolidated Financial Statements
December 31, 2007 and 2006

3. CHANGES AND DEVELOPMENTS IN ACCOUNTING POLICIES (CONTINUED)

Held-for-trading financial investments are measured at fair value and all gains and losses are included in net income in the period in which they arise. Available-for-sale financial instruments are measured at fair value with revaluation gains and losses included in other comprehensive income until the assets are removed from the balance sheet. All changes in the fair value of derivatives are recognized in earnings unless specific hedge criteria are met in accordance with Section 3865 which requires that a company must formally document, designate and assess the effectiveness of transactions that receive hedge accounting.

As a result of the adoption of these standards, the company designated its cash and cash equivalents as held-for-trading. Held-for-trading financial assets are measured at fair value with unrealized gains and losses recognized in the consolidated statement of income and other comprehensive income. Accounts receivable are classified as loans and receivables, which are measured at amortized cost. Accounts payable and accrued liabilities are classified as financial liabilities, which are measured at amortized cost.

The company classifies derivative instruments, such as foreign exchange forward contracts and foreign exchange options contracts, as held-for-trading unless the instruments meet all the criteria of a hedge. If the criteria are met, then any unrealized gains and losses will be reported in other comprehensive income.

Accounting Policy Developments

Capital Disclosures and Financial Instruments – Disclosure and Presentation

Effective January 1, 2008, the Company will adopt new accounting standards that were issued by the CICA for Capital Disclosures (“Section 1535”) and Financial Instruments (“Sections 3862 and 3863”).

Under Section 1535, the Company will disclose its objectives, policies and procedures for managing capital, whether the Company has complied with any externally imposed capital requirements and, if the Company has not complied with them, any consequences of non-compliance with these capital requirements.

The new Sections 3862 and 3863 replace Section 3861 (“*Financial Instruments – Disclosure and Presentation*”). Disclosure requirements are revised and enhanced, while presentation requirements remain essentially unchanged. The new disclosure requirements will expand discussion around the significance of financial instruments for the Company’s financial position and performance, the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date and how the entity manages those risks.

Goodwill and Intangible Assets

In February, 2008, the CICA issued Handbook Section 3064 (“*Goodwill and Intangible Assets*”), replacing Section 3062 (“*Goodwill and Other Intangible Assets*”), and Section 3450 (“*Research and Development Costs*”). The new Section 3064 addresses when an internally developed intangible asset meets the criteria for recognition of an asset.

TELEHOP COMMUNICATIONS INC.
Notes to the Consolidated Financial Statements
December 31, 2007 and 2006

3. CHANGES AND DEVELOPMENTS IN ACCOUNTING POLICIES (CONTINUED)

The Section also issued amendments to Section 1000 (“Financial Statement Concepts”). These changes are effective for fiscal years on or after October 1, 2008. The Company is currently evaluating the effects of adopting these changes.

Convergence with International Financial Reporting Standards

In February, 2008, The Canadian Accounting Standards Board confirmed that convergence to International Reporting Standards (IFRS) will be required in Canada. The Company will be required to report using IFRS beginning January 1, 2011 for interim and annual financial statements. The Company has begun the process of evaluating the impact of the change to IFRS.

4. CASH AND CASH EQUIVALENTS

	2007	2006
Operating cash	\$ 446,602	\$ 414,651
Short-term investments	2,435,703	2,364,013
	\$ 2,882,305	\$ 2,778,664

Short-term investments consist of term deposits and bankers acceptances with maturities less than three months. No asset-backed commercial papers were held at any time during the year.

5. INCOME TAXES

Income tax expense

The income tax expense for the years ended December 31, 2007 and 2006 are as follows:

	2007	2006
Current	\$ 149,146	\$ 541,708
Future	(36,766)	(157)
	112,380	541,551
Prior years' income tax reassessment	63,404	-
	\$ 175,784	\$ 541,551

TELEHOP COMMUNICATIONS INC.
Notes to the Consolidated Financial Statements
December 31, 2007 and 2006

5. INCOME TAXES (CONTINUED)

Future income taxes

Future income tax assets and liabilities as at December 31, 2007 and 2006 were as follows:

	2007	2006
Future income tax liability		
Accounting base of property and equipment in excess of tax value	\$ 32,284	\$ 69,050
Long-term	\$ 32,284	\$ 69,050

Reconciliation of provisions to statutory rates

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

	2007	2006
Net income before income taxes	\$ 348,532	\$ 1,565,733
Approximate applicable statutory tax rate	36.12%	36.12%
Income taxes at statutory tax rates	125,890	565,543
Prior years' reassessments	63,404	-
Other	(13,510)	(23,992)
	\$ 175,784	\$ 541,551

6. PROPERTY AND EQUIPMENT

	2007			2006		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Telecom equipment	\$ 1,191,183	\$ 766,404	\$ 424,779	\$ 1,411,966	\$ 832,583	\$ 579,383
Telecom switch equipment	-	-	-	938,139	938,139	-
Telecom equipment under capital lease	66,105	4,861	61,244	-	-	-
Computer software	262,330	117,609	144,721	284,756	120,853	163,903
Computer Equipment	27,327	4,878	22,449	1,544	386	1,158
Leasehold improvements	162,947	98,575	64,372	190,539	152,408	38,131
Furniture and equipment	114,499	62,718	51,781	100,694	76,948	23,746
Automobile	-	-	-	12,889	9,667	3,222
	\$ 1,824,391	\$ 1,055,045	\$ 769,346	\$ 2,940,527	\$ 2,130,984	\$ 809,543

Amortization expense for the year ended December 31, 2007 was \$318,289 (2006 - \$303,363). During the year, fully amortized assets totalling \$1,381,340 were removed from cost and accumulated amortization. Amortization expense relating to assets under capital lease was \$4,861.

TELEHOP COMMUNICATIONS INC.
Notes to the Consolidated Financial Statements
December 31, 2007 and 2006

7. INTANGIBLE ASSETS

	2007			2006		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Internally Developed	\$ 687,268	\$ 461,851	\$ 225,417	\$ 634,633	\$ 329,075	\$ 305,558
Software Licenses	53,664	11,627	42,037	53,664	894	52,770
	\$ 740,932	\$ 473,478	\$ 267,454	\$ 688,297	\$ 329,969	\$ 358,328

Amortization expense for the year ended December 31, 2007 was \$143,509 (2006 - \$117,185).

8. CAPITAL LEASE OBLIGATIONS

The company entered into a lease during the year for telecommunications equipment that had been capitalized. The security value of the capital equipment is \$77,771, and the maturity date of the lease is September, 2011.

	2007	2006
Total minimum lease payments	\$ 72,910	\$ -
Less: amount representing imputed interest of 6.2%	10,472	-
Present value of obligations under capital lease	62,438	-
Current portion - due within one year	15,253	-
Long-term obligations under capital lease	\$ 47,185	\$ -

9. SHAREHOLDERS' EQUITY

Authorized:

An unlimited number of common shares issued and outstanding

The changes in common shares for 2007 and 2006 are as follows:

	2007		2006	
	No. of Shares	Amount	No. of Shares	Amount
Balance, beginning of year	12,703,500	\$ 1,277,968	12,437,000	\$ 1,200,419
Issued on exercise of employee stock options (Note 9(a))	660,000	249,209	266,500	77,549
Balance, end of year	13,363,500	\$ 1,527,177	12,703,500	\$ 1,277,968

TELEHOP COMMUNICATIONS INC.
Notes to the Consolidated Financial Statements
December 31, 2007 and 2006

9. SHAREHOLDERS' EQUITY (CONTINUED)

(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. In the event of a reorganization, consolidation or change in control, the optionee has the right to exercise the share option.

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

	2007		2006	
	Number of options	Weighted Average Exercise Price	Number of options	Weighted Average Exercise Price
Options outstanding, beginning of year	1,115,000	\$ 0.26	1,289,500	\$ 0.26
Options granted	200,000	0.70	100,000	0.37
Options exercised	(660,000)	0.25	(266,500)	0.20
Options cancelled	(300,000)	0.31	(8,000)	0.20
Options outstanding, end of year	355,000	\$ 0.55	1,115,000	\$ 0.26
Options exercisable, end of year	155,000	\$ 0.35	1,085,000	\$ 0.25

TELEHOP COMMUNICATIONS INC.
Notes to the Consolidated Financial Statements
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9. SHAREHOLDERS' EQUITY (CONTINUED)

The following table summarizes information about stock options outstanding at December 31, 2007:

Options Outstanding			Options Exercisable	
Weighted Average Exercise Price	Number Outstanding	Weighted Average Remaining Contractual Life (years)	Number Exercisable	Weighted Average Exercise Price
\$ 0.32	5,000	1.94	5,000	0.32
\$ 0.35	150,000	0.72	150,000	0.35
\$ 0.60	100,000	4.98	-	0.60
\$ 0.80	100,000	4.76	-	0.80
	355,000	3.08	155,000	0.55

Options granted vest over a period not exceeding two years. All stock options granted have an exercise price equal to the fair market value at the grant date.

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

	December 31, 2007 Weighted Average	December 31, 2006 Weighted Average
Estimated fair value at the date of grant for options granted in the period	\$0.32 - \$0.80	\$0.30 - \$0.50
Assumptions utilized:		
Risk-free interest rate	4.25%	3.90%
Expected volatility	70%	72%
Expected life of the options	5 years	5 years
Expected Dividend Yield	3.5%	0%

(b) *Contributed surplus*

The following is a continuity of the changes in contributed surplus for the year ended December 31, 2007:

	2007	2006
Balance, beginning of year	\$ 174,261	\$ 154,819
Stock-based compensation expense (forfeited) during the year	(49,063)	43,692
Allocated to share capital on exercise of options during the year	(84,709)	(24,250)
Balance, end of year	\$ 40,489	\$ 174,261

TELEHOP COMMUNICATIONS INC.
Notes to the Consolidated Financial Statements
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10. EMPLOYEE FUTURE BENEFITS

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

	Registered Pension Plans	
	2007	2006
Change in benefit obligations		
Projected benefit obligation, beginning of year	\$ 353,900	\$ 308,414
Current service cost	55,800	47,921
Interest cost	20,163	27,147
Actuarial (gains) losses	18,500	(29,582)
Projected benefit obligation, end of year	448,363	353,900
Change in fair value of plan assets		
Fair value of plan assets, beginning of year	237,168	161,592
Return on plan assets	2,108	19,682
Employer contributions	58,673	55,894
Employee contributions	39,026	-
Fair value of plan assets, end of year	336,975	237,168
Funded status (plan deficit)	(111,388)	(116,732)
Unamortized net actuarial (gain) loss	17,267	-
Unamortized past service costs	138,075	150,628
Unamortized transitional (asset) obligation	(25,638)	(27,610)
Valuation allowance	-	-
Accrued benefit asset (liability)	18,316	6,286

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10. EMPLOYEE FUTURE BENEFITS (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	
	2007	2006
Current service cost	\$ 55,800	\$ 47,921
Interest cost	20,163	27,147
Actual return on assets	(2,108)	(19,682)
Actuarial loss on accrued benefit obligation	-	-
Elements of employee future benefit plans cost, before recognizing its long-term nature	73,855	55,386
Actuarial loss	-	-
Difference between the actual return and estimated return on plan assets	-	-
Amortization of transitional asset (obligation)	(1,972)	-
Amortization of past service cost	12,553	12,553
Amortization of net actuarial loss	1,233	(1,972)
Others	-	-
Adjustment to recognize long-term nature of employee future benefit plans credit	11,814	10,581
Increase in valuation allowance	-	-
Net benefit plans cost recognized	\$ 85,669	\$ 65,967

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

	2007	2006
Discount rate	5.6%	7.5%
Expected long-term rate of return on plan assets	7.5%	7.5%
Rate of compensation increase	3.0%	5.5%

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11. EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted earnings per share:

	2007	2006
Net Income	\$ 172,748	\$ 1,024,182
Weighted-average shares for earnings per share	12,874,497	12,508,844
Effect of dilutive securities Employee stock options	60,088	310,040
Adjusted weighted-average shares and assumed conversions for diluted earnings per share	12,934,585	12,818,884
Earnings per share	\$ 0.01	\$ 0.08
Diluted earnings per share	\$ 0.01	\$ 0.08

12. 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 Canada. 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.

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12. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT (CONTINUED)

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, 2007 and 2006, 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.

The net foreign exchange loss for 2007 was \$49,426 (2006 \$14,932) and has been recorded in general and administration expenses.

Foreign Exchange Contracts

The Company enters into forward foreign exchange contracts ("Forwards") and foreign exchange options contracts ("Options") 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. The Options allow the Company to exercise the right to purchase US dollars at pre-determined exchange rates for a pre-determined future period.

As at December 31, 2007, the Company did not enter into any Forwards or Options.

13. COMMITMENTS

Operating Leases

The Company has operating leases for its switch facility and corporate office. The future minimum payments under operating leases as at December 31, 2007 are as follows:

2008	\$	197,997
2009		197,997
2010		197,997
2011		165,673
	\$	<u>759,664</u>

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13. COMMITMENTS (CONTINUED)

Capital Leases

The future minimum payments under capital leases as at December 31, 2007 are as follows:

2008	\$	19,443
2009		19,443
2010		19,443
2011		14,581
	\$	<u>72,910</u>

14. RELATED PARTY TRANSACTIONS

- (i) The Company is recovering overpayments made to the Chairman from prior years, and a one-time \$12,000 salary adjustment in 2007. The balance is being repaid through bi-weekly instalments starting June 1, 2007 for the overpayments, and December 1, 2007 for the salary adjustment. As of December 31, 2007, the outstanding balance receivable is \$76,489, which is included in Accounts Receivable.
- (ii) Development costs totalling \$114,345 were expensed during the year to a company owned by an employee of the Company. The amount was recorded based on the exchange value and was included in development and technical expenses.

15. SUBSEQUENT EVENTS

- (i) In February, 2008, a management change was made by the Company in which the Chairman replaced the President and Chief Operating Officer (COO) in overseeing daily operations. Severance arrangements for the President and COO are pending as settlement negotiations are in progress.
- (ii) In March, 2008, the Company granted 50,000 stock options to an officer. The options have an exercise price of \$0.75, a term of 5 years and vesting restrictions. In the event of a reorganization, consolidation or change in control, the optionee has the right to exercise the stock option.

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16. CONTINGENT LIABILITY

- (i) The Company is in negotiations with a former executive involving a dispute that pertains to 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 continuing to bring closure to this settlement with the former executive. The final settlement amount is currently not determinable.

- (ii) In February, 2008, the Company received a notice of claim from a vendor for marketing services it believes the Company was committed to pay. The amount of the claim against the Company is \$231,629. The Company is vigorously defending such claims as it strongly believes it had never made such commitments. The litigation is in its preliminary stages and the outcome is not currently determinable. No amount has been recorded in relation to this claim.

17. COMPARATIVE FIGURES

Certain comparative figures have been reclassified from statements previously presented to conform to the current presentation.