

## MANAGEMENT'S DISCUSSION AND ANALYSIS

For the three and nine months ended September 30, 2011

**Dated November 22, 2011**

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 three and nine months ended September 30, 2011, compared with the operating results for the three and nine months ended September 30, 2010. The MD&A should be read in conjunction with the Unaudited Interim Consolidated Financial Statements for the three and nine months ended September 30, 2011. This MD&A is based on financial statements that reflect the adoption of International Financial Reporting Standards ("IFRS"). Our consolidated financial statements for the previous fiscal year were presented in accordance with previous Canadian Generally Accepted Accounting Principles ("GAAP"). All financial amounts, unless otherwise indicated, are in Canadian dollars and in accordance with IFRS.

### **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, and timing of product introductions, competition, and the ability of Telehop to attract and retain key employees. Readers are cautioned not to place undue reliance on forward-looking statements as various factors could cause actual future results, conditions or events to differ materially from expectations or estimates expressed in the forward-looking statements.



## **FINANCIAL REVIEW AND LOOKING FORWARD**

The first nine months of 2011 have seen significant changes and improvements which will better position the company to move forward:

- Management changed in April, bringing a new brand of leadership focused on marketing and operational improvements,
- Shareholders ratified the Company's direction during its AGM in May of this year,
- 25% Rights issuance was fully subscribed raising additional capital in late September,

Subsequent to the period end:

- Purchase agreement with a major Telecommunications company to replace the Company's existing and aging switch technology amounting to approximately \$450,000. The new switch will provide "carrier-grade" technology to enhance the quality of the Company's existing services,
- Three-year leasing agreement with a major Telecommunications company to house the new switch and enhance the Company's existing network infrastructure.

In order to ensure minimum impact to customer experience, it is necessary that the Company runs a duplicate network nationwide during implementation of the new switch. This will result in additional fourth quarter expenses amounting to approximately \$90,000. The completion date for the new switch project is expected to be in the first quarter of 2012.

Furthermore, the Company has overcome lingering Cash Flow commitments through fulfillment of its financial obligation to the Estate of its Founder and reaching settlement with an outstanding marketing litigation.

With new management engaged, and moving into the fourth quarter and beyond, the Company's focus will be to continue to grow and drive sales of subscription services namely, Long Distance, VoIP Phone, and High Speed Internet. The marketing strategy will focus on aggressively expanding the Company's network of Agents to move into new market segments. Furthermore, the company will continue to dedicate focus on the Research & Development of new products and services for launch in early 2012.

## **COMPANY OVERVIEW**

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's core network resides in Toronto, Ontario, with virtual points-of-presence in major cities across Canada. Revenues are earned from the access to, and the use of, our telecommunications network and infrastructure. One type of long distance service is sold, packaged in different forms, which includes casual calling, subscriptions, wholesale and VoIP – Telehop HomePhone and prepaid calling cards.

### *Casual Calling*

Telehop's 10-10-100 and 10-10-620 services allow customers to make long distance calls from their local phone service line without having to subscribe to the service, or pay any monthly fees. Casual Calling, also known as dial-around 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. What makes 10-10-100 and 10-10-620 unique for consumers is the pricing strategy. 10-10-100 is designed for users who make shorter calls and want to pay low per-minute pricing, whereas 10-10-620 is attractive to those consumers who want to enjoy longer calls for at a price of \$1.00 or \$1.99 for unlimited minutes or a certain block of minutes depending on the calling destination.

### *Subscriptions*

Equal Access – The Company is a provider of "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+' dialling pattern.

### *Wholesale*

Telehop's wholesale service is based on trading bulk minutes worldwide with high volume users who wish to carry their calls through our network. These high volume users often repackage the minutes purchased from us at discounted rates with their own unique services which are then sold to their customers.

### *VoIP - Telehop HomePhone*

Using Voice Over Internet technology, Telehop HomePhone is a feature packed service that's affordable and reliable. Customers are able to choose the home phone plan that best suits their lifestyle as well as bundle with any of our Telehop Long Distance plans and High Speed Internet plans. Our feature-packed home phone plans come with benefits at no extra cost:

- 8 calling features included
- Customers can keep their current number or pick a new number with the area code of their choice
- Expanded local calling area – they won't have to pay long distance rates to call within the Greater Toronto Area
- FREE calling to other Telehop Home Phone lines
- Travel with their home phone

Small and medium business customers will also benefit from our competitive Biz Phone rates and flexible Long Distance Biz bundles.

### *Prepaid Calling Cards*

The Company offers prepaid long distance calling cards using a toll free number to access the Company's network to make a long distance call. Revenue recognition is deferred until the customer has accessed and used the Company's network or the time allotment on the card expires.

## **KEY PERFORMANCE INDICATORS (KPI's) AND NON-GAAP MEASURES**

The Company measures its success through a number of key performance indicators, which are outlined below. The following key performance indicators are not measurements in accordance with IFRS and should not be used as an alternative to net income or any other measure of performance under IFRS.

### *Gross Margin*

Gross margin is determined by deducting all telecommunications-related expenses from operating revenues. Telecommunications expenses include fixed and variable carrier costs, billing and collections charges to local exchange carriers and support costs for all telecommunications facilities. Gross margin is an indicator of the company's profit directly tied to its services before general operating expenses.

### *Calls and Minutes*

Calls and minutes are determined by the number of calls and minutes that have been completed by customers through the Company's network, which are tracked through call detail records. This indicator is a measure of how well the Company has increased overall volume in customer usage of its network.

### *Average Revenue per Minute (ARPM)*

Average revenue per minute is determined by dividing total operating revenues by total number of minutes completed. This indicator serves to measure how well the company has maintained or increased its long-distance rates per minute.

### *EBITDA*

Earnings before interest, taxes, depreciation and amortization (EBITDA) is a standard used in the telecommunications industry to assist in understanding and comparing operating results. The Company believes that this measure is important in assessing its profitability before the impact of depreciation and amortization and non-operating factors. EBITDA is also a useful measure of the Company's ability to service debt, invest in capital equipment or distribute dividends to its shareholders. EBITDA is not defined by IFRS and should be used as a supplement and not a substitute for the Company's results of operations.

## RESULTS OF OPERATIONS

Consolidated Highlights (\$Thousands except for KPI's)	Three months ended		Nine months ended	
	Sept. 30, 2011	Sept. 30, 2010	Sept. 30, 2011	Sept. 30, 2010
<b>Consolidated Income Statement</b>				
Operating revenues	\$ 2,701	\$ 2,907	\$ 8,019	\$ 8,889
Gross margin	1,206	1,282	3,518	3,775
Gross margin %	44.7%	44.1%	43.9%	42.5%
Operating costs				
General and administration	636	600	2,027	1,893
Marketing and selling	524	372	1,335	1,193
Development and technical	128	213	530	642
Amortization	41	71	131	223
(Gain) loss on disposal of equipment	-	-	(1)	4
Interest	1	1	3	5
Operating income (loss)	\$ (124)	\$ 25	\$ (506)	\$ (186)
EBITDA	(83)	97	(374)	46
Other income	2	1	3	2
Net income (loss)	(76)	13	(384)	(158)
Earnings (loss) per share – basic	(0.01)	0.00	(0.03)	(0.01)
<b>Consolidated Statement of Cash Flows</b>				
Cash provided (used) by operating activities			\$ (306)	\$ (333)
Cash used by investing activities			(16)	(20)
Cash provided (used) by financing activities			275	(17)
<b>Key Performance Indicators</b>				
Minutes (thousands)	55,964	59,761	167,514	176,678
Calls (thousands)	11,566	14,767	37,305	43,090
Average revenue per minute (ARPM)	\$ 0.0483	\$ 0.0486	\$ 0.0479	\$ 0.0503

## OVERALL PERFORMANCE

### *Operating Revenues*

#### *Comparison of revenue by Core Business Product Line*

	<b>For the quarters ended September 30</b>			
	<b>2011</b>	2010	<b>+/-</b>	<b>%</b>
Retail revenue	<b>\$ 2,380,059</b>	\$ 2,560,913	\$ (180,854)	(7.1)%
Wholesale	<b>320,611</b>	346,512	(25,901)	(7.5)%
Total revenues	<b>\$ 2,700,670</b>	\$ 2,907,425	\$ (206,755)	(7.1)%

	<b>For nine months ended September 30</b>			
	<b>2011</b>	2010	<b>+/-</b>	<b>%</b>
Retail revenue	<b>\$ 7,061,666</b>	\$ 7,783,460	\$ (721,794)	(9.3)%
Wholesale	<b>957,598</b>	1,105,983	(148,385)	(13.4)%
Total revenues	<b>\$ 8,019,264</b>	\$ 8,889,443	\$ (870,179)	(9.8)%

Consolidated operating revenues declined quarter to quarter by \$206,755 or 7.1% this is a positive indication that revenue declines are being arrested as the third quarter 2010 report indicated the comparable declines were 14.2%.

A similar trend is showing in the year to date operating revenues, declining by 870,179 or 9.8% vs. the 14.7% decline reported in 2010 year to date figures. The initiatives put in place by the new management team in the second quarter 2011 are starting to stabilize the sales.

#### *Retail Revenue*

There has been a concerted effort to convert customers from Casual Calling to a paid Subscription basis or home phone. This effort is paying off and combined with Telehop's engaging new Call Centers for outbound telesales has resulted in an increase in the number of subscribers for our Subscription business. Our plan is to market Telehop HomePhone (VoIP), to these subscribers and new customers.

#### *Wholesale revenue*

Wholesale revenue has a significantly lower gross margin than the other lines of business. Wholesale customers buy "bulk minutes" from Telehop at discounted prices. This line of business is very competitive and margins for the overall Canadian market in this segment have declined. The Company is aggressively pursuing new Wholesale clients, in a highly competitive marketplace.

The Company is focusing on development of its retail sales through new sales channels and focusing strategic marketing of its products to the public.

### Gross Margin

	<b>September 30, 2011</b>	September 30, 2010	+/-	%
For the three months ended	<b>\$ 1,206,356</b> <b>44.7%</b>	\$ 1,282,450 44.1%	\$ (76,096) 0.6%	(5.9)%
For the nine months ended	<b>\$ 3,518,447</b> <b>43.9%</b>	\$ 3,775,121 42.5%	\$ (256,674) 1.4%	(6.8)%

The margin increased by 1.5% in the quarter as a result of improvements in our fixed network costs and faster cuts to more cost effective secondary vendors during peak operating hours.

Year to date gross margin as a % of revenue has increased by 1.4% from 42.5% in 2010 to 43.9% this year.

The acquisition of the new switch will improve margins in the first quarter of 2012, improved quality of the Homephone services and it will allow for expansion into new markets which have been as yet been unavailable to the Company. During the fourth quarter, while the new switch is being implemented, the company will experience a small decline in Gross margin levels in order to maintain uninterrupted service to its customers while transition to the new technology takes place.

### Operating Expenses

#### For the three months ended September 30

	<b>2011</b>	2010	+/-	%
General & administration	<b>\$ 635,883</b>	\$ 600,369	\$ (35,514)	(5.9)%
Marketing & selling	<b>523,906</b>	371,816	(152,090)	(40.9)%
Development & technical support	<b>128,084</b>	213,077	84,993	39.9%
Amortization	<b>40,927</b>	70,710	29,783	42.4%
Interest	<b>1,138</b>	1,197	59	4.9%
Operating expenses	<b>\$ 1,329,938</b>	\$ 1,257,169	\$ (72,769)	(5.8)%

Overall operating expenses of \$1,329,938 or 5.8% more than the third quarter 2010. We measure expenses on a total basis, monitoring them very closely and adjusting them where it is felt they are required. The changes in operating expenses by line item are discussed below.

General & administration expenses of \$635,883 have increased by \$35,514 or 5.9% from the \$600,369 incurred for the third quarter 2010. Other than the legal settlement discussed in Note 13 of the financial statements, generally these expenses have declined quarter over quarter.

Marketing and selling expenses of \$523,906 represents an increase of \$152,090 or 40.9%. The third quarter saw the implementation of two third party call centers targeting customer acquisition and consequently leading to increased upfront commissions, the revenues lag behind this type of campaign and management is monitoring the effectiveness of this endeavour on an ongoing basis.

Development and technical support expenses decreased by \$84,933 or 39.9% quarter to quarter from \$213,077 to \$128,84. This is an adjustment of staffing levels for the on-going support of our network.

Amortization expenses decreased by \$29,783 or 42.4% compared to the same period last year. The decrease was mainly driven by certain assets that became fully amortized in 2011.

**For the nine months ended  
September 30**

	<b>2011</b>	2010	+/-	<b>%</b>
General & administration	<b>\$ 2,027,364</b>	\$ 1,899,613	\$ (127,751)	(6.7)%
Marketing & selling	<b>1,334,726</b>	1,192,983	(141,743)	(11.9)%
Development & technical support	<b>526,662</b>	642,413	115,751	18.0%
Amortization	<b>130,636</b>	216,561	85,925	39.7%
Loss on disposal of equipment	<b>(1,451)</b>	3,758	5,209	138.6%
Interest	<b>3,492</b>	3,976	484	12.2%
Operating expenses	<b>\$ 4,024,429</b>	\$ 3,959,304	\$ (65,125)	(1.6)%

Included in the nine months operating expenses were the following significant items: start up costs associated with its calling card division, special meeting costs, duplicate salaries and severance costs on re-organization.

*EBITDA and Operating Income*

Comparing quarters EBITDA declined to \$(81,517) from \$96,649 and operating loss increased to \$(123,582) from a profit of \$25,282 relative to the same period last year.

Year to date EBITDA declined to \$(373,305) from \$(45,832) and operating loss increased to \$(502,757) from \$(186,197) as compared to the 2010.

## QUARTERLY RESULTS SUMMARY

The following table sets forth certain unaudited consolidated statements of operation for the most recent quarters of operations ending September 30, 2011. The operating results for any quarter are not necessarily indicative of results for any future period:

Summary of results (\$000's)	2011 IFRS			2010 Restated to IFRS				2009 Cdn. GAAP
	Q3	Q2	Q1	Q4	Q3	Q2	Q1	Q4
Revenue	2,701	2,647	2,671	2,869	2,907	3,060	2,922	2,970
Telecommunication costs	1,494	1,474	1,533	1,566	1,625	1,758	1,731	1,805
Gross margin	1,206	1,174	1,139	1,303	1,282	1,302	1,190	1,165
Gross margin as a %	45%	44%	43%	45%	44%	43%	41%	39%
Operating expenses								
General & administrative	636	727	664	608	600	665	632	910
Marketing & selling	524	399	411	435	372	404	417	473
Development & technical support	128	189	212	206	213	212	217	242
	1,288	1,315	1,287	1,293	1,254	1,281	1,266	1,625
EBITDA	(82)	(142)	(149)	55	98	21	(76)	(461)
Amortization	41	36	54	44	71	77	75	77
Interest expense	1	1	1	3	2	3	2	4
Unusual item	-	-	-	-	-	-	-	(676)
Other income	2	-	1	2	1	1	-	1
Income (loss) before tax	(122)	(179)	(202)	10	26	(58)	(153)	(1,205)
Income tax (recovery)	(46)	(29)	(44)	125	13	5	(44)	(291)
Net income (loss)	(76)	(145)	(158)	(115)	15	(63)	(108)	(914)
Earnings (loss) per share	(0.01)	(0.01)	(0.01)	(0.01)	0.00	0.00	(0.01)	(0.07)

## FINANCIAL CONDITION

The following table presents the variations in the Consolidated Statement of Financial Position after nine months ended September 30, 2011 as compared to December 31, 2010:

(\$000's)	Sept. 30 2011	Dec. 31 2010	Changes	
<b>Current Assets</b>				
Cash and cash equivalents	427	474	(47)	-9.9%
Accounts receivable	2,424	2,370	54	2.3%
Provision for doubtful accounts	(357)	(308)	(49)	15.9%
Inventory	5	-	5	n/a
Prepaid expenses and deposits	68	150	(82)	-54.7%
<b>Non-Current Assets</b>				
Deferred income taxes	333	214	119	55.6%
Property and equipment	230	308	(78)	-25.3%
Intangible assets	37	72	(35)	-48.6%
<b>Current Liabilities</b>				
Accounts payable and accrued liabilities	1,739	1,737	2	0.1%
Provisions	93	138	(45)	-32.6%
Obligations under capital lease	7	20	(13)	-65.0%
<b>Non-Current Liabilities</b>				
Obligations under capital lease	18	23	(5)	-21.7%
<b>Total shareholders' equity</b>	<b>1,309</b>	<b>1,362</b>	<b>(53)</b>	<b>-3.9%</b>

## CAPITAL RESOURCES AND LIQUIDITY

Since December 31, 2010, during the third quarter and net of the rights proceeds the Companies working capital we decrease by \$83,998 as compared to \$271,316 during the first half of the year from \$790,154 at December 31, 2010 to \$434,840 at September 30, 2011.

Capital expenditures for the nine months ended September 30, 2011 were \$15,555 compared with \$20,209 for the comparable period in 2010.

We manage liquidity risk to maintain sufficient liquid financial resources to fund our balance sheet and meet our commitments and obligations in the most cost-effective manner possible.

Late in September the company received proceeds from the fully subscribed rights offering amounting to \$292,344 after various expenses of \$41,431.

### *Leases*

We have long-term lease agreements for our corporate office and switch facility, both of which expire in late 2011 or mid 2012 and lease of office equipment which expires in 2015.

## Sources and Uses of Cash

The Company's cash flows from operating, investing and financing activities, as presented in the consolidated statements of cash flows, are summarized in the following table:

<b>Nine month periods ended Sept. 30</b> (thousands except ratios)	<b>2011</b>	<b>2010</b>	<b>\$ Change</b>	<b>% Change</b>
Cash provided (used) by operating activities	(306)	(337)	31	9%
Cash used in investing activities	(16)	(20)	4	20%
Cash used by financing activities	275	(13)	288	2215%
Decrease in cash	(47)	(370)	323	87%
Cash and cash equivalents	427	458	(31)	-7%
Current assets	2,567	2,738	(171)	-6%
Current liabilities	1,840	1,669	171	10%
Working capital	727	1,069	(342)	-32%
Current ratio	1.4	1.6	n/a	-13%

During the third quarter and net of the proceeds of the rights offering, the Company's cash position increased by \$125,405 to \$134,602 at September 30, 2011 the Company remains without any bank debt. This was the first quarter without a cash drain in paying obligations as they relate to the estate of our founder.

## Capitalization

As at June 30, 2011 the Company had 16,738,750 common shares outstanding and 850,000 share options, which are exercisable at an average strike price of \$0.154 per share prior to May 2016.

## FIRST TIME ADOPTION OF IFRS

Our accounting policies presented in Note 3, *Significant Accounting Policies*, have been applied in preparing the financial statements for the three months ended March 31, 2011, the comparative information for the period ended March 31, 2010, the year ended December 31, 2010 and the opening statement of financial position at January 1, 2010, our date of transition to IFRS. We have applied IFRS 1 – First-time Adoption of IFRS in preparing the consolidated statement of financial position as at January 1, 2010. The effects of the transition to IFRS on equity and total comprehensive income are presented in this note. Prior to January 1, 2010, our consolidated financial statements were prepared in accordance with previous Canadian GAAP.

## FIRST-TIME ADOPTION ELECTIONS

IFRS 1, First-time adoption of international financial reporting standards sets forth guidance for the initial adoption of IFRS. We are required to establish our IFRS accounting policies in accordance with standards in effect on our first annual reporting date, December 31, 2011. We are required to apply these policies retrospectively to determine the IFRS opening balance sheet at our date of transition, January 1, 2010. In addition, IFRS 1 provides both mandatory and optional exemptions to this general rule. We have chosen to apply certain exemptions to reduce the complexity involved in converting to IFRS, as the cost of not applying the exemptions would far outweigh the benefit to the users of our financial statements.

The significant exemptions that we have applied upon adoption are summarized below:

a) *Business combinations*

IFRS 1 indicates that a first-time adopter may elect not to apply IFRS 3, Business combinations, retrospectively to business combinations that occurred before the date of transition to IFRS. Applying IFRS 3 retrospectively would require a significant amount of analysis and work to restate business combination transactions that have occurred since our inception. We will elect to apply IFRS 3 to business combinations that occur on or after January 1, 2010.

b) *Estimates*

In accordance with IFRS 1, an entity's estimates under IFRS at the date of transition to IFRS must be consistent with estimates made for the same date under previous GAAP, unless there is objective evidence that those estimates were in error. Our IFRS estimates as of March 31, 2011, are consistent with our Canadian GAAP estimates for the same date.

c) *Expected areas of significance*

IFRS employs a conceptual framework that is similar to Canadian GAAP. However, significant differences exist in certain matters of recognition, measurement, and disclosure. While adoption of IFRS will not change our actual cash flows, it will result in changes to our reported financial position and results of operations. Set out below are the significant accounting differences that will impact our consolidated financial statements. The manner of presentation of certain items under IFRS has not been affected for clarity of this reconciliation only.

The following unaudited reconciliations present the identified differences between Canadian GAAP and IFRS for our consolidated opening balance sheet at January 1, 2010, and our consolidated statement of earnings for the year ended December 31, 2010. The reconciliations and comments are intended to highlight the most significant areas and should not be regarded as complete or final:

## RECONCILIATION OF PREVIOUS CANADIAN GAAP TO IFRS

Consolidated Statement of Financial Position (unaudited)	December 31, 2009 Cdn GAAP	Notes	Transition to IFRS	January 1, 2010 IFRS	December 31, 2010 IFRS
ASSETS					
CURRENT					
Cash and cash equivalents	\$ 827,412		-	\$ 827,412	\$ 473,712
Accounts receivable	2,424,306	A	\$ 309,381	2,733,687	2,369,973
Provision for doubtful accounts	-	A	(309,381)	(309,381)	(307,878)
Income taxes recoverable	150,682		-	150,682	-
Future income taxes	200,205	B	(200,205)	-	-
Prepaid expenses and deposits	107,137		-	107,137	149,807
	3,709,742		(200,205)	3,509,537	2,685,614
DEFERRED INCOME TAXES	-	B	200,205	200,205	214,293
PROPERTY AND EQUIPMENT	476,974	C, D	35,053	512,027	308,339
INTANGIBLE ASSETS	118,746		-	118,746	72,347
	\$ 4,305,462		\$ 35,053	\$ 4,340,515	\$ 3,280,593

Consolidated Statement of Financial Position (cont'd) (unaudited)	December 31, 2009 Cdn. GAAP	Notes	Transition to IFRS	January 1, 2010 IFRS	December 31, 2010 IFRS
<b>LIABILITIES</b>					
<b>CURRENT</b>					
Accounts Payable and accrued liabilities	\$ 2,657,444	A	\$ (98,509)	\$ 2,558,935	\$ 1,737,377
Provisions	-	A	98,509	98,509	138,145
Obligations under capital lease	16,526	C	5,925	22,451	19,938
	2,673,970		5,925	2,679,875	1,895,460
DEFERRED INCOME TAXES	10,717	B	-	10,717	-
OBLIGATIONS UNDER CAPITAL LEASE	12,395	C	29,127	41,522	22,869
	2,697,082		35,053	2,732,135	1,918,329
<b>SHAREHOLDERS' EQUITY</b>					
SHARE CAPITAL	1,553,456		-	1,553,456	1,553,456
CONTRIBUTED SURPLUS	85,816		-	85,816	119,248
ACCUMULATED COMPREHENSIVE INCOME (LOSS)	-		-	-	(5,481)
RETAINED EARNINGS (DEFICIT)	(30,892)		-	(30,892)	(304,959)
	1,608,380		-	1,608,380	1,362,264
	\$ 4,305,462		\$ 35,053	\$ 4,340,515	\$ 3,280,593

Consolidated Income Statement (unaudited)	December 31, 2010 Cdn. GAAP	Notes	Effect of transition	December 31, 2010 IFRS
OPERATING REVENUES	\$ 11,758,098		\$ -	\$ 11,758,098
Telecommunications costs	6,679,660		-	6,679,660
GROSS MARGIN	5,078,438		-	5,078,438
<b>OPERATING EXPENSES</b>				
General and administration	2,513,026	C	(7,628)	2,505,398
Marketing and selling	1,627,657		-	1,627,657
Development and technical support	848,506		-	848,506
Amortization	259,213	C, D	8,609	267,822
Interest	6,204	C	1,703	7,907
	5,254,606		2,684	5,257,290
OPERATING INCOME (LOSS)	(176,168)		(2,684)	(178,852)
Other income	3,517		-	3,517
INCOME (LOSS) BEFORE INCOME TAXES	(172,651)		(2,684)	(175,335)
Income taxes (recovery)	98,742		-	98,742
NET INCOME (LOSS)	(271,393)		(2,684)	(274,077)
Other comprehensive income (loss)	(5,481)		-	(5,481)
Comprehensive income (loss)	\$ (276,874)		\$ (2,684)	\$ (279,558)

The effect of transition to IFRS is explained below:

(A) *Provisions*

Under Canadian GAAP, accounts payable, accrued liabilities and provisions are combined on the balance sheet as a single line item. This is also true on the receivables side. Under IFRS provisions are required to be disclosed separately.

(B) *Future income tax asset/liability*

Under Canadian GAAP, future income tax assets and liabilities are classified as current or non-current as appropriate. Under IFRS, all future income tax assets and liabilities are classified as non-current.

(C) *Leases*

Under Canadian GAAP, certain rules allow leases of equipment to be classed as operating and expensed without recognizing the asset or obligation. Under IFRS, all leases are considered capital in nature. Assets under capital leases are amortized on a straight-line basis over the period of expected use for the class of asset leased. Obligations are recorded under the lease and reduced by lease payments net of imputed interest.

(D) *Plant and equipment*

Under Canadian GAAP, assets not in service do not get amortized until they are put into service. Under IFRS, assets are amortized from the point at which they become “available for use”.

**Reconciliation of Total Comprehensive Income (Loss) three months ended September 30, 2010:**

<b>Consolidated Income Statement (unaudited)</b>	<b>September 30, 2010 Canadian GAAP</b>	<b>Notes</b>	<b>Effect of transition</b>	<b>September 30, 2010 IFRS</b>
OPERATING REVENUES	\$ 2,907,425		\$ -	\$ 2,907,425
Telecommunications costs	1,624,974		-	1,624,974
<b>GROSS MARGIN</b>	<b>1,282,451</b>		<b>-</b>	<b>1,282,451</b>
OPERATING EXPENSES				
General and administration	602,276	C	(1,907)	600,369
Marketing and selling	371,816		-	371,816
Development and technical support	213,077		-	213,077
Amortization	68,557	C, D	2,153	70,710
Interest	770	C	427	1,197
	<b>1,256,496</b>		<b>673</b>	<b>1,257,169</b>
OPERATING INCOME (LOSS)	25,955		(673)	25,282
Other income	725		-	725
INCOME (LOSS) BEFORE INCOME TAXES	26,680		(673)	26,007
Income taxes (recovery)	13,111		-	13,111
NET INCOME (LOSS)	13,569		(673)	12,896
Other comprehensive income (loss)	-		-	-
Comprehensive income (loss)	\$ 13,569		\$ (673)	\$ 12,896

## Reconciliation of Total Comprehensive Income (Loss) nine months September 30, 2010:

Consolidated Income Statement (unaudited)	September 30, 2010 Canadian GAAP	Notes	Effect of transition	September 30, 2010 IFRS
OPERATING REVENUES	\$ 8,889,443		\$ -	\$ 8,889,443
Telecommunications costs	5,114,323		-	5,114,323
GROSS MARGIN	3,775,120		-	3,775,120
OPERATING EXPENSES				
General and administration	1,899,613	C	(5,721)	1,893,892
Marketing and selling	1,192,983		-	1,192,983
Development and technical support	642,413		-	642,413
Amortization	216,561	C, D	6,457	223,018
(Gain) loss on sale of equipment	3,758		-	3,758
Interest	3,976	C	1,277	5,253
	3,959,304		2,013	3,961,317
OPERATING INCOME (LOSS)	(184,184)		(2,013)	(186,197)
Other income	1,861		-	1,861
INCOME (LOSS) BEFORE INCOME TAXES	(182,323)		(2,013)	(184,336)
Income taxes (recovery)	(26,191)		-	(26,191)
NET INCOME (LOSS)	(156,132)		(2,013)	(158,145)
Other comprehensive income (loss)	-		-	-
Comprehensive income (loss)	\$ (156,132)		\$ (2,013)	\$ (158,145)

## Reconciliation of Equity as at September 30:

(unaudited)	Notes	Sept. 30, 2011	January 1, 2011	December 31, 2010	Sept. 30, 2010
Shareholders equity under previous GAAP		\$ 1,313,832	\$ 1,362,264	\$ 1,364,938	\$ 1,476,744
IFRS conversion		(2,684)	(2,684)	-	
Adjustments to shareholders equity to conform with IFRS:					
Obligations under lease	C	(564)	-	(752)	(564)
Property and equipment	D	(1,449)	-	(1,922)	(1,449)
Shareholders equity under IFRS		\$ 1,309,135	\$ 1,359,580	\$ 1,362,264	\$ 1,474,731

## RISKS AND RISK MANAGEMENT

The following areas summarize the principal risks and uncertainties that could affect Telehop's future results.

### Competition

Telecommunications providers are continually increasing the range of services they offer as well as lowering their long-distance rates to become more competitive. Telehop intends on mitigating these risks through offering more innovative solutions that will distance the Company from the price sensitive market, and further reduce its cost structure in anticipation of future price declines.

### Technology

The market for the Company's 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 the Company's business and operating results. A substantial portion of the Company's revenues are derived and expected to continue to be derived from providing telecommunications services that are based upon today's leading technologies and that are capable of adapting to future technologies.

#### *Regulatory*

Regulatory changes issued by the Canadian Radio and Telecommunications Commission (CRTC) could have a material adverse impact on Telehop's procedures, costs and revenues. The company is federally regulated by the CRTC and Industry Canada. The CRTC regulates certain tariff charges in which Telehop pays to certain local carrier exchanges and may issue changes which may have a material unfavourable impact on the Company's financial results. To mitigate these risks, the Company monitors industry developments very closely through industry advisors.

#### *Management Team*

Telehop operates with a small but effective and experienced management team that strives to oversee all aspects of operations, and by calling upon the services of financial, industry and technology experts when deemed appropriate.

The replacement of any management team member may have an adverse impact on operating results as their experience and skills may be difficult to find and match in the event of a management change. However, all team members are encouraged to document each of their key tasks and responsibilities as a means of mitigating this risk.

#### *Niche Company*

As a niche telecommunications long-distance provider serving primarily ethnic communities, the Company at this time does not have the full diversification in services compared to other larger telecommunications companies. Therefore, the Company is exposed to unforeseen changes in the long-distance market which could adversely affect the Company's future financial results. To mitigate these risks steps have been taken toward being a more diversified company by offering not only long-distance services but as a provider of additional telecommunications services.

#### *Foreign Exchange*

The Company's functional currency is the Canadian dollar, but it regularly transacts in U.S. dollars for a portion of its business activities. The assets, liabilities, revenues and expenses denominated in U.S. dollars will be affected by changes in the exchange rate fluctuations in the market between the Canadian and U.S. dollar.

The Company makes use of foreign currency forward contracts and options contracts to fix the exchange rates on the U.S. dollar to mitigate its foreign exchange exposure on expenses. From time to time the Company makes use of foreign currency forward contracts and options contracts to fix the exchange rates on the U.S. dollar to mitigate its foreign exchange exposure on expenses. As at June 30, 2011 the Company did not possess any foreign currency forward contracts.

#### *Credit*

The Company is subject to credit risk through accounts receivables, which consists of amounts represented by the large number of subscription services customers which are invoiced directly, and amounts owed from various ("Local Exchange Carriers") LEC's from casual calling revenues.

More than 50% of the Company's accounts receivables are owed by a few LECs across Canada. The LEC's provide billing and collection services on behalf of the Company through billing and collections agreements. Credit risks are mitigated from this group of LECs by purchasing long-distance services from them, which offsets at least 50% of the accounts receivables.

## **CONTINGENT LIABILITIES**

From time to time the Company has been, and expects to continue to be, subject to legal proceedings and claims in the ordinary course of our business. Such claims, even if lacking merit, could result in the expenditure of significant financial and managerial resources. The Company is not aware of any legal proceedings or claims that it believes will have, individually or in the aggregate, a material adverse effect on the Company's financial condition or results of operation.

## **DISCLOSURE CONTROLS**

Disclosure controls and procedures are designed to provide reasonable assurance that material information is gathered and reported to senior management, including the Chief Executive Officer (CEO) and Chief Financial Officer (CFO) until the date of his departure, as appropriate to permit timely decisions regarding public disclosure.

Management, including the CEO, have evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as of September 30, 2011. Based on this evaluation, the CEO and CFO have concluded that the Company's disclosure controls and procedures, as defined in Multilateral Instrument 52-109 – Certification of Disclosure in Issuer's Annual and Interim Filings, are effective except as below noted, to ensure that the information required to be disclosed in reports that are filed or submitted under Canadian Securities legislation are recorded, processed, summarized and reported within the time period specified in those rules.

During the process of review and evaluation it was determined that certain weaknesses existed in the disclosure controls and procedures. As is indicative of many small companies, segregation of duties and the existence of full competencies in the complex areas of revenue recognition were identified as areas requiring improvement. The existence of these weaknesses is compensated for by the senior management and Audit Committee monitoring which exists and in the case of complex transactions, by consulting with external experts to assist management in their analysis. The Company is taking steps to augment and improve the procedure and controls impacting these areas of weakness.

The Company does not expect that its disclosure controls and procedures will prevent all error and all fraud, if any. A control procedure, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control procedure are met. Because of the inherent limitations in all control procedures, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The Company considered these limitations during the development of its disclosure controls and procedures and will periodically re-evaluate them to ensure they provide reasonable assurance that such controls and procedures are effective.