**MANAGEMENT'S DISCUSSION AND ANALYSIS**
For the year ended December 31, 2005
**Dated April 27, 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, 2005 compared with the operating results for the year ended December 31, 2004. The MD&A should be read in conjunction with the Audited Consolidated Financial Statements for the year-ended December 31, 2005.

## 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 four sections:

- Telehop's Strategy & Business
- Highlights
- Overall Performance
- Outlook

## Telehop's Strategy & 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 Bell 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 its "HOP" long distance telephone services (currently marketed to the southern Ontario 'Golden Horseshoe' and the Metropolitan Montreal communities), 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 Q1 of 2005 Telehop launched its 10-10-100 service in Ontario, a second casual calling service based on per-minute billing. Telehop plans to roll out the 10-10-100 services to the west coast of Canada over the first two quarters of 2006.

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.

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

### “HOP” SERVICE

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

By maintaining switches at numerous points-of-presence in individual towns in its “Superhop” area, Telehop uses its own proprietary network and gateway switches to provide unlimited long distance telephone calls within the Greater Toronto Area and Metropolitan Montreal for a fixed monthly fee. A caller calls a local access telephone number that acts as a gateway to the Company's system and then enters the number to be called. Using intelligent routing of the call, this call is then completed as a free local call, which would otherwise have been a long distance toll call. This service replaces a customer’s monthly variable long distance charges within the Superhop area, with a lower fixed monthly fee. This service is also bi-directional, in that anybody within the “Superhop” areas can call the Telehop Superhop customer free, by first dialing a local access number. Telehop’s system does not require its customers to use a PIN number because of the sophisticated authentication tools built into its system.

### “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 SERVICE

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 scaleable 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.

## 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.

## HIGHLIGHTS

Market conditions in 2005 continued with the 2004 trend where new service providers continued to enter the telecommunications industry, particularly in the long distance sector. New technologies and strong consumer demand continues to attract niche market service providers, generally putting pressure on selling prices and costs as companies strive to maintain market share and profit margins. Notwithstanding, in the year ended December 31, 2005, Telehop continued to increase its market share and substantially penetrated new markets. Revenues from 2004 to 2005 increased by $5.5 million. This increase was achieved through ongoing aggressive marketing efforts and the continuing strength of our wholesale operations which allowed us to negotiate more favourable rates with our major global carriers. This is a significant achievement in the face of increased competition.

Key developments for Telehop's 2005 year were:

- A significant increase in long-distance traffic of 110% in the total number of minutes carried and 214% in the total number of calls over 2004 traffic.
- A 36% increase in revenue, achieved in a year when industry trends continued to report declines in wireline long distance revenue and increasing wireless revenues.
- Maintenance of telecom costs as a percentage of revenue in spite of increased pressure on revenue per minute. This was achieved by close attention to detail using its advanced proprietary management information system Telehop successfully maintained its largest individual operating cost at 58% for 2004 and 2005. This equates to an increase in gross profit of approximately $2.2 million in 2005.
- Strong working capital of $2.1 million with no long-term debt. The reduction in cash was primarily due to the earlier reduction in accounts payable by $598,560 in anticipation of a conversion of our accounting system on January 1, 2006. Hence, this reduction was only a timing issue; otherwise, the cash balance would have been approximately $1.7 million. New capital expenditures foreseen for the year 2006 should be comfortably financed from internally generated cash flow.
- The successful launch of a new per-minute casual calling service, "10-10-100", in Ontario in early 2005.
- A return on equity of 21%, a 75% improvement over 2004

## Overall Performance

The Canadian landscape continued to exhibit explosive growth in the wireless segment with an increase of 17.5% at the end of 2004. The wireline segment, on the other hand, continued to exhibit a decline in revenues. As in 2004, competition in the casual calling arena continued to be fierce. In 2005, Telehop's main focus was to build on its revenues by increasing its market share through its casual calling services and through acquisition of equal access customers. Over the year 2005, Telehop increased its number of 'direct dial' subscription customers by 255% resulting in a 'direct dial' call revenue increase of 322% from January 2005 to December 2005. 2005 was also a year where Telehop saw its newly branded "10-10-100" 'dial-around' service grow the number of its unique users approximately six-fold from January 2005 to December 2005 with only a 6% decrease in unique users of Telehop's branded "10-10-620" dial around service.

Telehop's unique strengths include its efficiencies with respect to successful targeted marketing to specific niche markets. In addition, low infrastructure costs combined with no long-term debt enable Telehop to stay competitive. Its ultimate strength is in its employees with Telehop enjoying an extremely low attrition rate and an employee base, which is skilled and experienced. This enables Telehop to dynamically respond to fluctuating market situations and gives it the capability to translate direction to action in short time. Telehop continues to see the declining revenue per minute as a challenge to growth and will continue to focus on the addition of complementary value-added services that will enable it to derive greater revenue and greater profitability per customer. Furthermore, Telehop plans to work on creating a package that encompasses market needs to encourage loyalty.

Operating Results

For the year ended December 31, 2005 the overall financial and operating condition of the Company improved with specific regard to growing a more profitable revenue base and diversification of its product portfolio over the previous year.

The key factors were:

- A healthy mix of retail and wholesale revenues with a net improvement in gross margin of approximately $2.2 million over 2004
- Maintenance of telecom costs as a percentage of revenue of 58%, which is consistent with 2004
- A decrease in general and administration costs of 1.1% as a percentage of revenue over the previous year
- A return on equity of 21%, a 75% increase from 2004. This was a result of Telehop's ability to finance its operations entirely from equity and retained earnings.
- Improvement in working capital from 1.63 in 2004 to 2.10 in 2005 – a net improvement of $0.55 million.

All these factors are described in detail below.

Most of the Canadian telecom Companies continued to show a trend towards declining long distance revenues in spite of modest increases in traffic through their systems. Due to a global oversupply of capacity, the per-minute rates for long distance traffic have shown steady declines over the past few years.

In 2005, Telehop's focus was to increase its retail revenues. Telehop was successful in increasing its total traffic minutes by 110% or 170 million minutes over 2004 ending the year with a total of 326.2 million minutes. The total number of calls also increased significantly with 44.3 million calls more than in 2004, translating to a 214% increase over the previous year, for a total of 65.0 million calls in 2005 versus 20.7 million calls in 2004. Telehop saw a decrease in revenues per minute from 10 cents per minute in 2004 to 6 cents per minute in 2005. This was attributed to an intentional increase in wholesale traffic that brings in lower revenues per minute. However, this strategy has allowed Telehop to significantly increase its purchasing power with its major global carriers.

## REVENUE

Total revenue in 2005 increased substantially over 2004, with an increase of $5.5 million. This increase in revenue was attributed to significant increases in Telehop's "subscription" customer base as well as increased wholesale revenues.

## CARRIER CHARGES AND OPERATING COSTS

| ($ thousands) | | | Variance | | Revenue % | |
|---|---|---|---|---|---|---|
| | 2005 | 2004 | $ | % | 2005 | 2004 |
| **Revenue** | 20,817 | 15,326 | 5,491 | 35.8% | 100.0% | 100.0% |
| **Telecom costs** | 12,082 | 8,810 | 3,272 | 37.1% | 58.0% | 57.5% |
| **Gross profit** | 8,735 | 6,516 | 2,219 | 34.1% | 42.0% | 42.5% |
| **Operating costs** | 7,335 | 5,522 | 1,813 | 32.8% | 35.2% | 36.0% |
| **EBITDA *** | 1,400 | 994 | 406 | 40.8% | 6.7% | 6.5% |
| **Depreciation** | 419 | 435 | (16) | | | |
| **Interest** | 3 | 9 | (6) | | | |
| **Taxes** | 367 | 265 | 102 | | | |
| **Net Income** | 611 | 285 | 326 | | | |
| **EPS** | $ 0.05 | $ 0.02 | | | | |
| **Diluted EPS** | $ 0.05 | $ 0.02 | | | | |

*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.

### *Telecom costs*

In spite of a 110% increase in minutes and a 214% increase in the total number of calls carried, Telehop's total telecom costs remained flat as a percentage of revenue for the years 2005 and 2004.

Fixed telecom costs decreased by 1% of revenue in 2005 over 2004.This is attributed to optimum and effective utilization of the network.

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.

Telehop's increase in minutes has added to its improved base business, enabling it to negotiate better bulk rates with its major global carriers.

### *Operating Costs*

**General & administration** costs increased by $0.66 million in 2005, representing a 1.2% decrease as a percentage of revenue over 2004. This decrease is attributed to the implementation of revised compensation structures for management as well as improved efficiencies within the company.

**Marketing and selling expenses** increased in 2005 by $1.0 million or 0.8% as a percentage of revenue over 2004, from $2.5 million in 2004 to $3.5 million in 2005. This increase in marketing and selling costs contributed significantly to the increase in revenues in 2005 of $5.5 million, with increased market share in competitive markets and strong market penetration in new target markets across Canada. The increase in marketing expenditures was primarily due to the launch of a new casual calling service, “10-10-100”, in Ontario as well as the launch of an aggressive campaign to acquire equal access subscribers across Canada.

**Development and technical support** increased by $0.09 million and remained flat as a percentage of revenue at 3% in 2005 and 2004. The main reason for the increase includes the expensing of the majority of software development done in the current year.

*FINANCIAL SUMMARY*

| | **2005** | 2004 |
|---|---|---|
| **Total revenue** | **20,817,340** | 15,325,613 |
| **Income** | **978,147** | 550,106 |
| **Net income** | **611,065** | 284,983 |
| **Net income per share** | **0.05** | 0.02 |
| **Diluted net income per share** | **0.05** | 0.02 |
| **Total assets** | **5,232,753** | 5,195,255 |
| **Total liabilities** | **2,001,166** | 2,589,634 |
| **Shareholders' equity** | **3,231,587** | 2,605,621 |
| **Return on equity** | **21%** | 12% |

SUMMARY OF QUARTERLY RESULTS

| | 2004 | | | | | 2005 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Q4 | Total | Q1 | Q2 | Q3 | Q4 | Total |
| | ($ thousands) | | | | | | | | | |
| **Revenue** | 3,643 | 3,624 | 3,921 | 4,138 | 15,326 | 4,720 | 5,062 | 5,571 | 5,464 | 20,817 |
| **EBITDA*** | 412 | (19) | 363 | 238 | 994 | 284 | 108 | 257 | 751 | 1,400 |
| **Income** | 306 | (130) | 244 | 130 | 550 | 173 | 4 | 150 | 651 | 978 |
| **Net income** | 190 | (90) | 145 | 40 | 285 | 110 | 3 | 96 | 402 | 611 |
| **Earnings per share** | | | | | | | | | | |
| **Basic** | 0.02 | (0.01) | 0.01 | 0.00 | 0.02 | 0.01 | 0.00 | 0.01 | 0.03 | 0.05 |
| **Diluted** | 0.02 | (0.01) | 0.01 | 0.00 | 0.02 | 0.01 | 0.00 | 0.01 | 0.03 | 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.

Telehop’s revenues show an increase over each corresponding quarters of 2004. This reflects the combination of successful marketing efforts and the rollout of new services across Canada. The last quarter in 2005 showed an increase of $1.3 million or 32% over the comparable quarter in 2004.

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 capital lease obligations of $14,363 will be repaid within the next 12 months. Total operating lease commitments are as follows:

| | |
|---|---|
| 2006 | 147,457 |
| 2007 | 177,984 |
| 2008 | 177,984 |
| 2009 | 177,984 |
| 2010 | 177,984 |
| Thereafter | 156,324 |
| | 1,015,717 |

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

Telehop currently has no bank debt, other long-term debt or any other off-balance sheet arrangements. At year end the Company had $0.83 million cash in the bank and the working capital ratio was 2.1:1.

***Cash flow***

In 2005 the Company generated cash from operating activities of $55,037, up from cash generated from operating activities of $19,968 in 2004.

The Company has adequate working capital to fund fiscal 2006 and foresees no requirement for outside financing at this point in the normal course.

The Company estimates that it currently has sufficient capacity to significantly expand the traffic through its system without incurring any major capital expenditures in the foreseeable future. Management views the keys to expanding traffic as being continued targeted marketing and careful and selective expense management.

At the end of 2005, Telehop had a cash balance of $832,735 and accounts receivable of $3,156,492 compared to cash of $1,262,491 and accounts receivables of $2,541,509 at the end of 2004. Total current assets at the end of 2005 were $4,051,078, which remained flat from $4,063,905 in 2004. The reduced cash balance in 2005 of $429,756 over 2004 is mainly the result of the earlier reduction in accounts payable by $598,560 in anticipation of a conversion of our accounting system on January 1, 2006. This was to ensure that we had sufficient time to correct any system problems related to the issuance of cheques. No problems were encountered after the conversion.

Book value of Property, plant and equipment and intangible assets increased by $50,325 after applying depreciation and amortization of $419,522 for the year giving total assets of $5,232,753 in 2005 compared to $5,195,255 in 2004. The increase is attributed mainly to acquisition of communication equipment to keep pace with new technology.

Cash was used to pay corporate taxes amounting to $314,661 and reducing accounts payable by $598,560. This resulted in total current liabilities of $1,931,959 in 2005, decreasing from 2004 by $565,703, while total current assets decreased marginally by $12,827, effectively improving the working capital by $552,876 over 2004.

Working capital at the end of 2005 totaled $2.1 million, a 35% improvement of $552,876 from the 2004 working capital of $1.6 million.

## CHANGES IN ACCOUNTING POLICIES

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 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.

Beginning January 1, 2004, the Company adopted the recommendations of the revised Section 3870, and has applied the recommendations of this section retroactively without restatement of prior periods. As a result, opening retained earnings as at January 1, 2004 has been decreased to reflect the expensing of the fair value of $16,763 and $85,597 for options granted to employees in 2002 and 2003 respectively

## 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 2005 $70,990 (2004 - $68,141)

## 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.

## FOURTH QUARTER 2005

Telehop's revenue for the three months ended December 31, 2005 was $5,464,998 compared with $4,137,897 in the same period in 2004. Net income in the 2005 fourth quarter increased by $362,257 from $39,852 ($0.00 per share) in 2004, to $402,109 ($0.05 per share) in 2005 as a result of sustained marketing and cost control focus. Telehop's revenue increase of $1,327,101 or 32% in the fourth quarter of 2005 over the fourth quarter of 2004 was due to the success in marketing efforts in gaining market share and penetrating new markets.

Telehop's total long distance traffic processed by the Company for Q4 in 2005 showed significant growth over the comparable quarter in 2004. The total long distance traffic for Q4 in 2005 increased to 86.7 million minutes in 18.5 million calls, versus a total of 48.9 million minutes in 6.6 million calls in the same quarter of 2004. This was attributed to the increase in wholesale traffic over 2004.

Telehop's total telecom costs increased from $2.5 million in Q4 of 2004 to $2.9 million in Q4 of 2005. This represented a decrease of 8% as a percentage of revenues over the comparative quarter and is attributable to aggressive cost control efforts realized through optimum network utilization. Fixed costs increased marginally from $344,427 in Q4 of 2004 to $423,758 in Q4 of 2005, a 0.05% decrease as a percentage of revenue in 2005 to 7.8% of revenue versus 8.3% of revenue in 2004.

General & administration costs for Q4 in 2005 increased by $210,936 over Q4 of 2004 with the percentage to revenue remaining flat over 2004.

Marketing and selling costs for Q4 in 2005 increased by $243,428 over Q4 of 2004. Marketing costs in Q4 of 2005 were $821,823 from $578,395 in Q4 of 2004 representing an increase of 1.1% as a percentage of revenue in Q4 of 2005 over Q4 of 2004; to 15.0% in Q4 of 2005 from 13.9% in Q4 of 2004. This increase contributed significantly to the 32% increase in revenue.

## CAPITALIZATION

As of April 22, 2006 the Company had 12,437,000 common shares outstanding and 1,289,500 common share purchase options, which are exercisable at prices ranging between $0.20 and $0.35 per share at varying times before June 24, 2010.

## RISKS RELATED TO 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**

Telehop expects to continue increasing its market share through effective niche marketing. In 2006, Telehop is placing increased focus on increasing profitability and providing added value to its shareholders.

This will be done by

- Increasing profitable revenue growth – by offering services that are in demand to new and existing customers, continuing to expand our footprint across Canada, and reaching new niche markets through specialized campaigns and affinity programs
- Increasing operating margins through:
    - maintaining tight controls on overhead costs.
    - dedicated network monitoring and optimization.
    - using our purchasing power to leverage telecommunications savings.

In summary, Telehop expects to see increased profitability through the year continuing the trend set in 2005. In addition, Telehop expects that its 2006 capital expenditure and customer acquisition marketing programs will be financed out of cash flow, although these expenditures could accelerate depending on market conditions or any acquisitions or other business opportunities that may arise.