



MANAGEMENT'S DISCUSSION AND ANALYSIS

For the year ended December 31, 2004

Dated May 2, 2005

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, 2004 compared with the operating results for the year ended December 31, 2003. The MD&A should be read in conjunction with the Audited Consolidated Financial Statements for the year-ended December 31, 2004.

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 carrier quality service to its customers. Telehop maintains its profitability by maintaining a very tight focus on 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 has also applied for a carrier's license to operate its services in New York State. Telehop currently employs approximately 40 people.

Telehop's core network resides in Toronto, Ontario, with virtual points-of-presence in major cities across Canada. The Maritime Provinces were launched in Q1 of 2005.

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 technology has to offer.

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. In Q3 of 2004, Telehop launched its 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. In the same quarter of 2004, Telehop introduced Directory Assistance services to its customer base through casual calling. This service offers operator-assisted Directory Assistance through the use of 10-10-620. In Q1 of 2005, 10-10-100, a second casual calling service based on per-minute billing was launched in Ontario.

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+. This year, 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 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.

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.

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.

"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 Competitive Local Exchange Carriers ("CLECs") across Canada.

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 10-10-620-0. The charges, as for casual calling, appear on the customer's regular monthly phone bill.

Highlights

2004 experienced an unprecedented influx of new service providers into the telecommunications industry, particularly in the long distance sector. New technologies and strong consumer demand has attracted 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, 2004, Telehop continued to increase its market share and made substantial progress in penetrating new markets. Revenues from 2003 to 2004 remained constant and this was achieved through a significant increase in marketing efforts with increased spending amounting to \$0.8 million from \$1.7 million in 2003 to \$2.5 million in 2004 consequently resulting in a decrease in net income from \$0.9 million in 2003 to \$0.3 million in 2004. The success of the marketing efforts resulted in Telehop's geographic growth and revenues in 2004 being higher in every quarter and year-over-year revenues staying relatively flat over 2003. Telecom costs, however, saw a decrease in 2004 of \$0.3 million over 2003, which represents a 3.3% improvement. This is a significant achievement in the face of increased competition.

Key developments for Telehop's 2004 year were:

- A significant increase in long-distance traffic of 12% in the total number of minutes carried and 16% in the total number of calls over 2003 traffic. This increase in traffic allowed Telehop to sustain its revenues even though the revenues per minute showed a decline from 11 cents per minute in 2003 to 10 cents per minute in 2004
- A significant increase in retail revenues to offset the decrease in wholesale revenues that resulted in 2004 revenue over 2003 remaining relatively flat. This decrease in wholesale revenues may be attributed to the business decision made toward the end of 2003 to reduce high-risk wholesale revenues to an acceptable level. The increase in retail revenue is a significant achievement in a year when industry trends continued to report declines in long distance revenue and increasing wireless revenues.
- Lowering 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 lowered its largest individual operating cost from 58.45% in 2003 to 57.48% of revenues in 2004, yielding a gross return of 42.5% in 2004 compared to 41.5% in 2003. This equates to an increase in gross profit of approximately \$40,000.
- Strong cash position of \$1.3 million with no long-term debt. Even though Cash decreased from \$1.6 million in 2003 to \$1.3 million in 2004, this includes taxes prepaid for 2004 amounting to \$155,240. New capital expenditures foreseen for the year 2005 should be comfortably financed from cash flow.
- Expansion of 1010620 and the direct dial (1+ service) into Saskatchewan and Manitoba as well as the signing of the Billing and Collection Agreements with Aliant for the provinces of New Brunswick, Nova Scotia, PEI, Newfoundland and Labrador.

- The launching of BroadTalk, Telehop's entry into the VoIP (Voice over Internet Protocol) market.
- The addition of Directory Assistance services on its casual calling network in Ontario and Quebec.
- The expansion of the flat rate network to include Montreal into its Ontario-wide network

Overall Performance

The Canadian telecom landscape changed in 2004 with the introduction of new disruptive technology in the form of Voice over Internet early in 2004. Through the year, the casual calling arena saw a number of new entrants making the market space more competitive than ever.

2004 was a challenging year for Telehop. Always striving to be in the forefront with respect to technology, Telehop launched its Voice over Internet service, BroadTalk in Q3 of 2004. With its vast experience in the casual calling market, Telehop decided to differentiate its offering by adding operator-assisted Directory Assistance, also in Q3 of 2004.

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 sees the declining revenue per minute as an obstacle to revenue growth and plans to add complementary value-added services that will enable it to derive greater revenue per customer. In addition, Telehop plans to create a portfolio of services that cater to its customers' needs and will work on creating a package that will encourage loyalty.

Operating Results

For the year ended December 31, 2004 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 \$40,000 or 1% over 2003
- A decrease in telecom costs of approximately \$0.3 million or 1% as a percentage of revenue over 2003
- A decrease in general and administration costs of approximately \$0.1 million over the previous year
- A seven fold return on marketing dollars expended towards the growth of retail revenues. The planned cutback on wholesale revenues necessitated this additional expense to enable Telehop to sustain its overall revenue.
- Improvement in working capital. Current assets increased in 2004 by \$0.1 million over 2003 and current liabilities decreased in 2004 by \$0.35 million over 2003 – a net improvement of \$0.45 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 2004, Telehop's focus was to increase its retail revenues to offset the planned cutback on its high-risk and low margin wholesale revenues. Telehop was successful in increasing its total traffic minutes by 12% or 17.2 million minutes over 2003 ending the year with a total of 155.5 million minutes. The total number of calls also increased significantly with 2.8 million calls more than in 2003, translating to a 16% increase over the previous year, for a total of 20.7 million calls in 2004 versus 17.9 million calls in 2003. In keeping with the continuing trend of declining revenues per minute, Telehop saw a nominal decrease in revenues per minute from 11 cents per minute in 2003 to 10 cents per minute in 2004. In spite of the decrease in revenue per minute, Telehop was successful in maintaining its revenues through increased traffic on its network. In order to further support its revenues, Telehop is expanding geographically.

In 2004, Telehop's expansion plan had included all of Canada and New York. This plan has since changed with Telehop focusing primarily on its Canadian expansion due to the strength of the Canadian dollar. Expansion into the US will be reviewed at a future date.

REVENUE

Total revenue in 2004 stayed relatively flat over the year 2003, with a nominal decrease of \$0.26 million. Even with a planned decrease of 59% in wholesale revenues, Telehop was successful in increasing its retail revenues by 7% as well as improving its gross margin by 1% over 2003. This increase in revenue is partly attributed to Telehop's increased footprint across Canada.

CARRIER CHARGES AND OPERATING COSTS

(\$ thousands)			Variance		Revenue %	
	2004	2003	\$	%	2004	2003
Revenue	15,326	15,588	(262)	-1.7%	100.0%	100.0%
Telecom costs	8,810	9,112	(302)	-3.3%	57.5%	58.5%
Gross profit	6,516	6,476	40	0.6%	42.5%	41.5%
Operating costs	5,522	4,685	837	17.9%	36.0%	30.1%
EBITDA *	994	1,791	(797)	-44.5%	6.5%	11.5%
Depreciation	435	315	120			
Interest	9	(1)	10			
Taxes	265	546	(281)			
Net Income	285	931	(646)			
EPS	\$ 0.02	\$ 0.08				
Diluted EPS	\$ 0.02	\$ 0.08				

*Earnings before Interest, Taxes, Depreciation and Amortization. EBITDA is a measure that has no standardized meaning prescribed by Canadian GAAP and is considered a non-GAAP measure. Therefore, the measure may not be comparable to similar measures presented by other issuers. This measure is described and presented in the MD&A, in order to provide

shareholders and potential investors with additional information regarding the Company's liquidity and ability to generate funds to finance its operations.

Telecom costs

In spite of a 12% increase in minutes and a 16% increase in the total number of calls carried, Telehop's total telecom costs decreased from \$9.1 million in 2003 to \$8.8 million in 2004, a total saving of approximately \$0.3 million. This represented a decrease of 1% as a percentage of revenues over 2003.

Fixed telecom costs decreased \$173,000 or 10% over 2003. This improvement in our biggest cost category was achieved despite increased fixed telecom costs related to the startup of operations in Saskatchewan and Manitoba.

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 global carriers.

Operating Costs

General & administration costs decreased by \$0.1 million in 2004 representing a 0.3% decrease as a percentage of revenue over 2003. This decrease is attributed to the efficiencies of tight cost control measures, staff training and development and strict adherence to departmental budgets.

Marketing and selling expenses increased in 2004 by \$0.8 million or 5% as a percentage of revenue over 2003, from \$1.7 million in 2003 to \$2.5 million in 2004. This increase in marketing and selling costs contributed to the maintenance of revenues in 2004 over 2003 with increased market share in competitive markets and strong market penetration in new target markets across Canada yielding a seven-fold return on marketing dollars expended in 2004 versus a twelve-fold return on marketing dollars expended in 2003. . The increase in spending was primarily due to new advertising and marketing costs in the provinces of Manitoba and Saskatchewan as well as the maintenance of a strong continued presence in Ontario, Quebec, BC and Alberta along with the launch of its two new services, BroadTalk and Directory Assistance.

Development and technical support increased by \$0.15 million to 3% of revenue in 2004 over 2% of revenue in 2003. The major reason for the increase includes the expensing of the majority of software development done in the current year.

FINANCIAL SUMMARY

	<u>2004</u>	<u>2003</u>
Total revenue	15,325,613	15,587,884
Income	550,106	1,477,153
Net income	284,983	930,672
Net income per share	0.02	0.08
Diluted net income per share	0.02	0.08
Total assets	5,206,337	5,138,923
Total liabilities	2,600,716	2,953,446
Shareholders' equity	2,605,621	2,185,477

SUMMARY OF QUARTERLY RESULTS

	2003					2004				
	Q1	Q2	Q3	Q4	Total	Q1	Q2	Q3	Q4	Total
	(\$ thousands)									
Revenue	3,908	4,055	3,859	3,766	15,588	3,643	3,624	3,921	4,138	15,326
EBITDA*	382	400	450	559	1,791	412	(19)	363	238	994
Income	312	320	368	477	1,477	306	(130)	244	130	550
Net income	181	192	226	332	931	190	(90)	145	40	285
Earnings per share										
Basic	0.01	0.02	0.02	0.03	0.08	0.02	(0.01)	0.01	0.00	0.02
Diluted	0.01	0.02	0.02	0.03	0.08	0.02	(0.01)	0.01	0.00	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.

Telehop's revenues in Q1 & Q2 of 2004 show a decrease over Q1 & Q2 of 2003 due to a decrease in low margin wholesale revenues. Wholesale revenues were reduced due to stricter credit policies being imposed by Telehop management. The remainder of the year shows the success of marketing efforts to increase retail revenue to offset the decrease in wholesale revenue with the last two quarters in 2004 generating Telehop's highest quarterly revenues this far. The last quarter in 2004 showed an increase of \$372,000 or 10% over the comparable quarter in 2003.

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 \$29,309 will be repaid within the next 12 months. Total operating lease commitments are as follows:

2005	145,656
2006	147,456
2007	177,984
2008	177,984
2009	177,984
Thereafter	334,308
	1,161,372

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 \$1.3 million cash in the bank and the working capital ratio was 1.6:1.

Cash flow

In 2004 the Company generated cash from operating activities of \$19,968, down from \$730,510 in 2003. The decrease is attributable to the decrease in net income in 2004 of \$645,689 over 2003 and the prepayment of 2004 corporate taxes amounting to \$155,240. This accelerated reduction in cash is evident only for 2004. Going forward, Telehop foresees a stronger cash position due to adequate provisioning for prepaid corporate taxes.

The Company has adequate working capital to fund fiscal 2005 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 2004, Telehop had a cash balance of \$1,262,491 and accounts receivable of \$2,541,509 compared to cash of \$1,631,587 and accounts receivables of \$2,287,095 at the end of 2003. Total current assets at the end of 2004 were \$4,063,905 up from \$3,951,919 in 2003. The reduced cash balance in 2004 of \$369,096 over 2003 is the net result of increased accounts receivables of \$254,414 over 2003 and taxes prepaid in 2004 amounting to \$155,240.

Book value of Property, plant and equipment and intangible assets decreased slightly after applying depreciation and amortization of \$435,178 for the year giving total assets of \$5,206,337 in 2004 compared to \$5,138,923 in 2003.

Cash was used to pay corporate taxes amounting to \$753,000. This resulted in total current liabilities of \$2,497,662 in 2004 decreasing from 2003 by \$340,314 while total current assets increased by \$141,370, effectively improving the working capital by \$452,300 over 2003.

Working capital at the end of 2004 totaled \$1.6 million, a 37% improvement of \$452,300 from the 2003 working capital of \$1.1 million.

LEGAL PROCEEDINGS

The Company is in receipt of an unissued statement of claim for proceedings against it by the former CFO for constructive dismissal in the amount of approximately \$125,000 plus miscellaneous costs.

The outcome cannot be determined at this stage and accordingly no provision has been recorded. In the opinion of the Company the claim is unjustified and will be vigorously defended.

The Company believes that the resolution of this proceeding will not have a material effect on its financial situation

TRANSACTIONS WITH RELATED PARTIES

A company owned by a significant shareholder provided managerial and consulting services in the amount of \$NIL in 2004(2003 - \$784,459). At the year-end \$NIL was owing in connection with these services. (2003 - \$399,133).

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 or 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 2004 \$68,141 (2003 - \$NIL)

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 2004

Telehop's revenue for the three months ended December 31, 2004 was \$4,137,799 compared with \$3,765,784 in the same period in 2003. Net income in the 2004 fourth quarter decreased by \$277,000 from \$332,000 (\$0.03 per share) in 2003, to \$55,000 (\$0.00 per share) in 2004 as a result of new technologies and entrants into the market resulting in tighter margins and increased costs. Telehop's revenue increase of \$370,000 or 10% in the fourth quarter of 2004 over the fourth quarter of 2003 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 2004 showed significant growth over the comparable quarter in 2003. The total long distance traffic for Q4 in 2004 increased to 48.9 million minutes in 6.6 million calls, versus a total of 31.5 million minutes in 3.9 million calls in the same quarter of 2003.

Telehop's total telecom costs increased from \$2.1 million in Q4 of 2003 to \$2.5 million in Q4 of 2004. This represented an increase of 5% as a percentage of revenues over the comparative quarter and is attributable primarily to the reduction of profit margins due to increased competition. Fixed costs reduced from \$534,000 in Q4 of 2003 to \$344,000 in Q4 of 2004, a 6% decrease as a percentage of revenue in 2004 to 8.3% of revenue versus 14.2% of revenue in 2003.

General & administration costs for Q4 in 2004 decreased by \$36,000 or 6% over Q4 of 2003, resulting in a 2.6% decrease as a percentage of revenues over 2003.

The percentage of marketing and selling costs to revenues for Q4 in 2004 increased by 3% to 14% in 2004 versus 11% in 2003. This increase is primarily due to the focus on replacing wholesale revenues with retail revenues as well as needing to service an expanded coverage area.

CAPITALIZATION

As of April 22, 2005 the Company had 12,437,000 common shares outstanding and 1,089,500 common share purchase options, which are exercisable at prices ranging between \$0.20 and \$0.35 per share at varying times before September 19, 2008.

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 that the current trend in growth in market share will continue. Special focus will be placed on the following in 2005 and beyond:

- 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 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 continued strong growth in total billable minutes carried, total number of calls, and in revenues and operating performance in 2005, as compared to 2004. In addition, Telehop expects that its 2005 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.