

Financial Statements of

**NATIONAL CAPITAL FREENET
INCORPORATED**

Year ended December 31, 2001



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AUDITORS' REPORT TO THE BOARD OF DIRECTORS

We have examined the statement of financial position of National Capital FreeNet Incorporated as at December 31, 2001 and the statements of operations, changes in net assets and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In common with many non-profit organizations, the Company derives revenue from donations and fundraising, the completeness of which is not susceptible of satisfactory audit verification. Accordingly, our verification of these revenues was limited to the amounts recorded in the records of the company and we were not able to determine whether any adjustments might be necessary to donations and fundraising revenue, deficiency of revenue over expenses, assets and net assets.

In our opinion, except for the effect of adjustments, if any, which we might have determined to be necessary had we been able to satisfy ourselves concerning the completeness of the revenue referred to in the preceding paragraph, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2001 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles. As required by the Canada Corporations Act, we report that, in our opinion, these principles have been applied on a consistent basis.

KPMG LLP

Chartered Accountants

Ottawa, Canada

February 15, 2002

NATIONAL CAPITAL FREENET INCORPORATED

Statement of Financial Position

December 31, 2001, with comparative figures for 2000

	2001	2000
Assets		
Current assets:		
Cash	\$ 36,550	\$ 39,857
Segregated cash (note 3)	26,060	58,783
Accounts receivable	5,735	1,050
Prepaid expenses	465	432
	<u>68,810</u>	<u>100,122</u>
Capital assets:		
Computer equipment	117,103	145,498
Telecommunications equipment	162,813	156,132
Systems software	238,220	100,139
Business equipment	8,075	7,033
	<u>526,211</u>	<u>408,802</u>
Less accumulated amortization	<u>309,161</u>	<u>274,814</u>
	<u>217,050</u>	<u>133,988</u>
	<u>\$ 285,860</u>	<u>\$ 234,110</u>

Liabilities and Net Assets

Current liabilities:		
Accounts payable and accrued liabilities	\$ 26,987	\$ 7,328
Deferred revenue (note 3)	26,060	58,783
	<u>53,047</u>	<u>66,111</u>
Deferred contributions related to equipment and software (note 2)	198,498	108,338
Net assets:		
Unrestricted	15,763	34,011
Invested in capital assets	18,552	25,650
	<u>34,315</u>	<u>59,661</u>
Commitment (note 4)		
	<u>\$ 285,860</u>	<u>\$ 234,110</u>

See accompanying notes to financial statements.

On behalf of the Board:

_____ Director

_____ Director

NATIONAL CAPITAL FREENET INCORPORATED

Statement of Operations

Year ended December 31, 2001, with comparative figures for 2000

	2001	2000
Revenue:		
Donations	\$ 159,397	\$ 167,411
Network projects	47,463	68,170
Amortization of deferred contributions (note 2)	57,103	38,515
Fundraising	269	7,265
	<hr/> 264,232	<hr/> 281,361
Expenses:		
Telecommunications	64,000	65,615
Network projects	53,022	63,263
Administration and professional fees	38,459	59,437
Office staff and supplies	41,798	44,950
Amortization of capital assets	64,742	44,239
Systems administration	27,301	29,597
Fundraising	256	1,773
	<hr/> 289,578	<hr/> 308,874
Deficiency of revenue over expenses	<hr/> \$ (25,346)	<hr/> \$ (27,513)

See accompanying notes to financial statements.

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Statement of Changes in Net Assets

Year ended December 31, 2001, with comparative figures for 2000

	Unrestricted	Invested in capital assets	2001 Total	2000 Total
Balance, beginning of year	\$ 34,011	\$ 25,650	\$ 59,661	\$ 87,174
Deficiency of revenue over expenses	(25,346)	—	(25,346)	(27,513)
Purchase of capital assets	(541)	541	—	—
Amortization of capital assets	64,742	(64,742)	—	—
Amortization of deferred contributions related to capital assets	(57,103)	57,103	—	—
Balance, end of year	\$ 15,763	\$ 18,552	\$ 34,315	\$ 59,661

See accompanying notes to financial statements.

NATIONAL CAPITAL FREENET INCORPORATED

Statement of Cash Flows

Year ended December 31, 2001, with comparative figures for 2000

	2001	2000
Cash provided by (used in):		
Operations:		
Deficiency of revenue over expenses	\$ (25,346)	\$ (27,513)
Items not involving cash:		
Amortization of deferred contributions	(57,103)	(38,515)
Amortization of capital assets	64,742	44,239
Changes in non-cash working capital items:		
Accounts receivable	(4,685)	4,290
Prepaid expenses	(33)	(180)
Accounts payable and accrued liabilities	19,659	(267)
Deferred revenue	(32,723)	58,783
	<u>(35,489)</u>	<u>40,837</u>
Investing activities:		
Contribution of capital assets	147,263	71,918
Contribution of capital assets put in service	(147,263)	(71,918)
Purchase of capital assets	(541)	(28,758)
	<u>(541)</u>	<u>(28,758)</u>
Increase (decrease) in cash and cash equivalents	(36,030)	12,079
Cash and cash equivalents, beginning of year	98,640	86,561
Cash and cash equivalents, end of year	<u>\$ 62,610</u>	<u>\$ 98,640</u>

The Company considers cash and cash equivalents to be highly liquid investments with original maturities of three months or less.

See accompanying notes to financial statements.

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Notes to Financial Statements

Year ended December 31, 2001

National Capital FreeNet Incorporated is a not-for-profit organization, the aims and objectives of which are to establish and operate a community based computer network to store, access and exchange information between individuals and organizations in the national capital region.

The Company was incorporated on September 29, 1992 under the Canada Corporations Act as a not-for-profit organization without share capital within the meaning of the Income Tax Act (Canada) and accordingly is exempt from income tax.

1. Significant accounting policies:

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The significant accounting policies are summarized as follows:

(a) Capital assets:

Purchased equipment and systems software are recorded at cost. Contributed equipment and software are recorded as a capital asset at fair value at the date of contribution. Contributed equipment and software are recorded as a deferred contribution and recognized as revenue at an amount equal to the related amortization on those assets.

Amortization is provided on the straight-line basis using an annual rate of 25%.

(b) Revenue recognition:

Project revenue to fund specific future project expense is deferred and recognized in the period in which the related expenses are incurred.

Donations are recognized in the year received.

(c) Contributed services:

Contributed services are recognized when a fair value can be reasonably estimated and when the services would otherwise have been purchased.

(d) Use of estimates:

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

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Year ended December 31, 2001

2. Deferred contributions:

Deferred contributions relate to the unrecognized portion of contributed equipment and software. The changes in the deferred contributions balance for the year are as follows:

	2001	2000
Balance, beginning of year	\$ 108,338	\$ 74,935
Add contributed equipment and software	147,263	71,918
Less amount recognized as revenue	(57,103)	(38,515)
Balance, end of year	\$ 198,498	\$ 108,338

3. Deferred revenue:

Deferred revenue includes revenue received for projects contracted for in the year and to be completed in the following year.

Details of the year-end balance are as follows:

	2001	2000
Office of Learning Technologies Thin Client Startup	\$ 26,060	\$ 50,615
Office of Learning Technologies Authenticated Webmail Expansion Services	–	8,168
	\$ 26,060	\$ 58,783

4. Commitment:

The Company is committed to payments under an agreement for telephone lines to May 31, 2003. Required annual payments are as follows:

2002	\$ 26,725
2003	11,135
	\$ 37,860