

PRELIMINARY PROSPECTUS DATED JUNE 12, 2000

THIS IS A PRELIMINARY PROSPECTUS RELATING TO THESE SECURITIES, A COPY OF WHICH HAS BEEN FILED WITH THE ONTARIO, QUEBEC, ALBERTA AND MANITOBA SECURITIES COMMISSIONS, BUT WHICH HAS NOT YET BECOME FINAL FOR THE PURPOSE OF A DISTRIBUTION TO THE PUBLIC. INFORMATION CONTAINED HEREIN IS SUBJECT TO COMPLETION OR AMENDMENT. THESE SECURITIES MAY NOT BE SOLD, NOR MAY OFFERS TO BUY BE ACCEPTED FROM RESIDENTS OF ANY SUCH PROVINCE PRIOR TO THE TIME A RECEIPT FOR THE FINAL PROSPECTUS IS OBTAINED FROM THE APPROPRIATE SECURITIES COMMISSION OR SIMILAR REGULATORY AUTHORITY IN SUCH PROVINCE.

This prospectus constitutes a public offering of these securities only in those jurisdictions where they may be lawfully offered for sale and therein only by persons permitted to sell such securities. No securities commission or similar authority in Canada has in any way passed upon the merits of the securities offered hereunder and any representation to the contrary is an offence. The securities offered hereby have not been and will not be registered under the United States Securities Act of 1933, as amended, and may not be offered or sold within the United States or to U.S. persons. See "Private Placement and Plan of Distribution".

New Issue

AXXENT INC.
(formerly, OCI Communications Inc.)
12,521,750 Class B Non-Voting Shares

This prospectus qualifies the issue and distribution of 10,000,000 Class B non-voting shares ("Class B non-voting shares") of Axxent Inc. (formerly, OCI Communications Inc.) ("Axxent Inc." or the "Company") to be issued without additional payment on the exercise of an aggregate of 10,000,000 special warrants of the Company (the "Special Warrants") previously issued by the Company on March 28, 2000.

This prospectus also qualifies the issue and distribution of up to an aggregate of 2,488,417 Class B non-voting shares of the Company to be issued upon the conversion of up to 2,488,417 Series 3 preferred shares ("Series 3 preferred shares") to be issued by the Company to holders of the senior notes of the Company's operating subsidiary, Axxent Corp. (formerly, Optel Communications Corporation), in exchange for warrants that such persons hold to purchase 2,488,417 common shares of Axxent Corp. Each Series 3 Preferred share is convertible into one Class B non-voting share upon payment by the holder of \$0.03 per share. In addition, this prospectus qualifies the issue and distribution of 33,333 Class B non-voting shares to be issued without additional payment on the exercise of an aggregate of 33,333 special warrants of the Company (the "Pathway Special Warrants") previously issued by the Company on February 11, 2000.

The holders of Class B non-voting shares of the Company are entitled to the benefit of "coattail provisions" that will give such holders specified rights in the event that a take-over bid meeting certain criteria is made for the Class A voting shares ("Class A voting shares") of the Company. See "Description of Share Capital – Coattail Provisions". The Company's articles of incorporation, as amended, impose certain restrictions on the ownership and transfer of the Company's Class A voting shares. See "Description of Share Capital – Restrictions on Non-Canadian Ownership and Control".

The Special Warrants were issued and sold to certain purchasers in accordance with applicable prospectus exemptions under securities legislation at a price of \$18.00 per Special Warrant pursuant to an underwriting agreement (the "Underwriting Agreement") dated March 28, 2000 among Axxent Inc., Griffiths McBurney & Partners, CIBC World Markets Inc., Credit Suisse First Boston Securities Canada Inc., Scotia Capital Inc. and Yorkton Securities Inc. (collectively, the "Underwriters"). The price of the Special Warrants was determined by negotiation between the Company and the Underwriters.

The Series 3 preferred shares will be issued to holders of the senior notes of the Company's operating subsidiary, Axxent Corp. (formerly, Optel Communications Corporation), in exchange for warrants that such persons held to purchase 2,488,417 common shares of Axxent Corp. See "Description of Certain Indebtedness – 1997 Notes". The

Pathway Special Warrants were issued by the Company on February 11, 2000 as partial consideration in connection with the acquisition of all of the issued and outstanding shares of Pathway Communications. See “Business of the Company – Acquisitions”.

The Special Warrants were issued pursuant to a special warrant indenture dated March 28, 2000 between Axxent Inc. and CIBC Mellon Trust Company (“CIBC Mellon”), as special warrant agent. Each Special Warrant entitles the holder thereof to receive, without payment of additional consideration, one Class B non-voting share (subject to adjustment in certain events). The Special Warrants are exercisable until, and will be deemed to be exercised without any further act on the part of the holder, at 5:00 p.m. (Toronto time) on the day (the “Expiry Date”) which is the earlier of: (i) the sixth business day after a receipt is issued in the province in which the holder of Special Warrants resides for the (final) prospectus (the “Final Prospectus”) qualifying the issuance of the Class B non-voting shares to be issued upon exercise of the Special Warrants; and (ii) 4:59 p.m. (Toronto time) on March 28, 2001. Any Special Warrants not exercised on or before 5:00 p.m. (Toronto time) on the Expiry Date shall be exercised immediately prior thereto by CIBC Mellon on behalf of the holder without any further action on the part of the holder. In the event that the Company has not received a receipt for the Final Prospectus from the securities regulatory authorities in each province in Canada where a holder of Special Warrants resides by July 31, 2000, each Special Warrant exercised after such date will entitle the holder thereof to 1.03 Class B non-voting shares without payment of any additional consideration.

The Company’s outstanding Class B non-voting shares are listed on The Toronto Stock Exchange (the “TSE”), under the trading symbol “AXI.B”. On March 13, 2000, the trading day immediately preceding the announcement of the offering of the Special Warrants, the closing price of the Class B non-voting shares on the TSE was \$20.50 per share. The TSE has conditionally approved the listing of the Class B non-voting shares to be qualified by this prospectus.

Resale restrictions apply to any Class B non-voting shares issued pursuant to the exercise of the Special Warrants prior to the issuance of a receipt for the Final Prospectus. The price of each Class B non-voting share issuable upon the exercise of the Special Warrants after giving effect to this issue exceeds the consolidated net tangible book value of such Class B non-voting share as at April 30, 2000, after giving effect to the exercise of the Special Warrants, by \$3.80 per Class B non-voting share, representing dilution of 69%. See “Dilution”. An investment in the securities qualified hereby is subject to certain risks and should be considered speculative. See “Risk Factors”.

	<u>Price to Purchaser</u>	<u>Underwriters’ Fees</u> ⁽¹⁾	<u>Net Proceeds to the Company</u> ⁽²⁾
Per Special Warrant	\$18.00	\$0.90	\$17.10
Per Pathway Special Warrant	\$6.06	Nil	\$6.06
Total	\$180,200,000	\$9,000,000	\$171,200,000

(1) No additional fee will be paid to the Underwriters in connection with the issue or transfer of Class B non-voting shares upon the exercise of Special Warrants.

(2) Before deducting the aggregate expenses of the Special Warrant Offering estimated to be \$705,008. See “Plan of Distribution”.

Certificates representing the Class B non-voting shares issuable upon exercise, deemed exercise or conversion, as the case may be, of the Special Warrants, the Series 3 preferred shares and the Pathway Special Warrants will be available for delivery on or about the time of such exercise, deemed exercise or conversion. Certain legal matters relating to the distribution of the Class B non-voting shares issuable upon exercise of the Special Warrants and the Pathway Special Warrants and the conversion of the Series 3 preferred shares are subject to approval of Wildeboer Rand Thomson Apps & Dellelce, LLP on behalf of the Company and by Blake, Cassels & Graydon LLP on behalf of the Underwriters.

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SUMMARY

The following is a summary only and is qualified in its entirety by the more detailed information contained in this prospectus. Unless the context otherwise requires, all references in this prospectus to "Axxent Inc." or the "Company" refer to Axxent Inc., its wholly-owned subsidiary, Axxent Corp., and Rhythms Canada Inc., its Canadian joint venture with Rhythms NetConnections, Inc. All dollar amounts in this prospectus are stated in Canadian dollars unless stated otherwise. Certain terms used in this Prospectus are defined in the Glossary.

Certain figures quantifying the size of the Canadian telecommunications market, and related segments of the total market, were prepared at the request of the Company, by Lemay-Yates Associates Inc. ("Lemay-Yates"), a telecommunications consulting firm located in Montreal, Quebec. Management believes that Lemay-Yates' analysis is based on reliable information (including Statistics Canada reports, ILEC (as hereinafter defined) tariffs, CRTC (as hereinafter defined) filings and public filings of telecommunications services providers) and that its assumptions are reasonable. There can be no assurance, however, that the Lemay-Yates analysis will not vary from actual results and that such variances will not be material.

The Company effected a consolidation of all of its outstanding Class A voting shares, Class B non-voting shares and options to purchase Class B non-voting shares on a three-for-one basis in connection with a capital reorganization on October 27, 1999. See "Capital Reorganization". All references to securities issued and prices paid for or payable in respect of such securities before such date have been adjusted to reflect such consolidation. Except where otherwise indicated, all information in this prospectus assumes (i) the March 1999 formation of Axxent Inc. as a holding company to hold all of the issued and outstanding shares of its operating subsidiary; (ii) completion of the consolidation of the Company's outstanding Class A voting shares, Class B non-voting shares and options to purchase Class B non-voting shares on a three-for-one basis; and (iii) the October 1999 amalgamation of the Company's subsidiaries, Pathway (as hereinafter defined) and CTRA (as hereinafter defined) with the Company's operating subsidiary.

Overview

Axxent Inc. (formerly, OCI Communications Inc.) is a rapidly growing Canadian telecommunications provider of bundled voice, data and Internet services. The Company targets small and medium-sized businesses, a sector that management believes to be under-served by the large telephone companies and that management believes has significant revenue and profit potential. According to Lemay-Yates, the total Canadian telecommunications market for voice, data and Internet services exceeded \$17.8 billion in 1999.

In order to facilitate its entrance into the local telecommunications market as early as possible, the Company began operations as a reseller of local telephone services in January 1995. Management believes this was the best way to enter the local services market as it enabled the Company to establish a customer base in order to capitalize on the lowering of unbundled local loop rates and the commencement of facilities-based competition in January 1998. The Company's revenues have increased from \$1.4 million for the fiscal year ended September 30, 1996 to \$45.9 million for the fiscal year ended September 30, 1999. For the six-month period ended March 31, 2000, Axxent Inc.'s revenues were \$29.9 million compared to \$21.3 million for the same period in the prior fiscal year. As of April 30, 2000, the Company had over 105,000 access lines in service and in excess of 25,000 business customers, of which 9,038 access lines and 1,516 customers were on the Company's network. Of these business customers, approximately 5,163 currently receive Internet and data services from Axxent Inc.

The Company was one of the first competitive local exchange carriers ("CLECs") to meet all of the requirements of the Canadian Radio-television and Telecommunications Commission (the "CRTC") to operate as a CLEC in Canada and was the first or one of the first CLECs to co-locate in the principal metropolitan centres of Toronto and Montreal. Axxent Inc. operates its own switching equipment in the Company's head office in Toronto as well as in the Company's Montreal office. Axxent Inc. has purchased, installed and is utilizing DMS-500 switching equipment purchased from Nortel Networks Corporation ("Nortel") to provide voice services in Toronto and Montreal and has purchased ATM switches from Cisco Systems Inc. ("Cisco Systems") for its data services. Within the first seven

months of establishing its own switching equipment, Axxent Inc. has successfully migrated 4,773 business access lines, representing 4.5% of its total business access lines, to its network. As of May 5, 2000, Axxent Inc. had 35 co-location sites in operation. The Company intends to offer facilities-based voice and data services in Canada's major markets outside of Toronto and Montreal, including Vancouver, Calgary, Quebec City, Ottawa-Hull, Kitchener-Waterloo, London and Hamilton. The Company's business plan calls for Axxent Inc. to have established co-location sites in 100 incumbent local exchange carrier ("ILEC") central offices in those markets by the end of fiscal 2000.

The Company believes that it is one of the first Canadian CLECs to offer high-speed data services using DSL-based technology. In January 2000, Axxent Inc. formed a joint venture with Rhythms NetConnections, Inc. ("Rhythms NetConnections"), one of the leading providers of DSL-based services in the United States, to create Rhythms Canada Inc. ("Rhythms Canada") and to develop a DSL-based network across Canada. Axxent Inc. has agreed to use Rhythms Canada products and services when marketing DSL-based data services to small and medium-sized businesses. The Company has structured the joint venture so that Axxent Inc., and not Rhythms Canada, has the right to market DSL-based data services to small and medium-sized business customers as well as certain specified large business customers. Rhythms Canada, through its own sales force, offers dedicated high-speed DSL-based services to large and wholesale customers, including ISPs, carriers and value-added resellers.

Network Design

The Company's network design is based on the use of DSL technology and its network deployment strategy is what is commonly referred to in the industry as a "smart build strategy".

Management believes that DSL technology will fundamentally change the economic structure of the telecommunications industry. When deployed, DSL equipment increases the data-carrying capacity of a standard copper telephone line (the "local loop") by up to 100 times. In addition, DSL technology can be used in voice applications to carry up to 24 voice lines simultaneously on a local loop, which management believes provides significant opportunity for margin improvement.

Using a smart build strategy, the Company will own only the strategic assets in its network, such as switches and customer premises equipment. This is in contrast to a traditional fibre build strategy where a carrier would build and own most, if not all, the assets in its network. In addition, the use of a smart build strategy requires less capital than a fibre build strategy, offers attractive gross margins, minimizes time to market and facilitates capital efficiency. See "Business of the Company – Business Strategy".

Axxent Inc. has entered into an equipment purchase agreement with Nortel which provides for the purchase of \$39.0 million of telecommunications equipment and services.

Market Opportunity

In May 1997, the CRTC deregulated local services by issuing a local competition decision (the "Local Competition Decision"). This decision enhanced the Company's market opportunity by opening Canada's local telecommunications market to facilities-based competition effective January 1, 1998. See "Regulation". Management believes that deregulation will result in the CLECs, including the Company, gaining a significant portion of the local market from the ILECs. According to Lemay-Yates, Canada's telecommunications services industry revenue, including local and long distance, was approximately \$17.8 billion in 1999, of which business services amounted to approximately \$11.7 billion.

Management believes that the growing demand for high-speed digital communications will make data services the fastest growing segment in the telecommunications market for many years to come. High-speed access has become important to small and medium-sized businesses due to the dramatic increase in Internet usage, the emergence of e-commerce, the need to maintain complex web sites and the desire to access critical business information. According to Lemay-Yates, Canadian telecommunications revenue attributable to the data services market, including revenue from Internet services net of carrier costs, was approximately \$4.2 billion in 1999, representing a compounded annual growth rate of 26% over 1996.

Business Strategy

The Company's goal is to become the telecommunications provider of choice for small and medium-sized businesses in Canada by offering bundled voice, data and Internet services. The Company has begun to deploy data capabilities in its network with the initial establishment of a DSL-based high-speed access network through Rhythms Canada. The key elements of the Company's business strategy include the following:

- *Capitalize on Favourable Economics of Smart Build Strategy Using DSL-Based Technology.* DSL-based technology allows Axxent Inc. to significantly improve its overall margins by increasing data carrying capacity and enabling Axxent Inc. to deliver multiple voice telephone lines to a customer over a single local loop. In addition, the Company's smart build strategy requires much less capital than would a fibre build strategy and facilitates capital efficiency, because much of the capital is deployed only after Axxent Inc. contracts with a customer.
- *Provide Integrated Services With a New Emphasis on Data.* The rapid growth of the Internet, expansion of e-commerce and the introduction of new business applications have fuelled increasing demand in the Company's target market for access to high-speed data services. The Company expects to be a single source provider of bundled telecommunications services by offering voice, data and Internet services.
- *Target Under-Served Small and Medium-Sized Business Market.* Customers in the Company's targeted small and medium-sized business market typically purchase telecommunications services from multiple vendors and do not have dedicated personnel with telecommunications expertise. Management believes that small and medium-sized businesses are currently under-served by the ILECs and would value a provider of integrated telecommunications services.
- *Leverage Axxent Inc.'s Early to Market Advantage.* Axxent Inc.'s early entry into the telecommunications market has afforded it advantages, including the following:
 - Axxent Inc. was one of the first CLECs to co-locate in the principal metropolitan centres of Toronto and Montreal;
 - Axxent Inc. believes that it is one of the first Canadian CLECs to offer high-speed data services using DSL-based technology; and
 - Axxent Inc. will utilize its in-house and contracted sales force to further penetrate target markets in advance of potential competitors.
- *Continue to Provide Superior Customer Service.* Through a commitment to customer service and innovative pricing and term contracts, Axxent Inc. has achieved customer loyalty and historically low customer attrition rates.
- *Leverage Sophisticated Back Office Systems.* The Company has implemented and is continuing to integrate a scalable operational support system that allows for the rapid provisioning of service, the highest level of customer support and accurate and timely billing. As a result of this integration, which management believes is the first of its kind in Canada, Axxent Inc. has developed a more efficient and streamlined customer service process.
- *Continue to Pursue Acquisitions and Strategic Alliances.* The pursuit of growth opportunities and strategic acquisitions of telecommunications companies in Canada is an element of the Company's business strategy. Acquisition opportunities will be considered by Axxent Inc. where the target has a technology, customer base or business complimentary to that of the Company.
- *Utilize the Experience of the our Management Team.* Axxent Inc. has built a strong management team with extensive experience in the Canadian telecommunications industry. The Company's management team is led by Robert Latham, its President and Chief Executive Officer, who has over 30 years experience in the telecommunications industry.

The Offering

Issuer:	Axxent Inc. (formerly, OCI Communications Inc.) (“Axxent Inc.” or the “Company”).
Offering:	12,521,750 Class B non-voting shares (subject to adjustment in certain events) to be issued by the Company upon the exercise of 10,000,000 special warrants issued on March 28, 2000 (the “Special Warrants”), 33,333 special warrants issued on February 11, 2000 (the “Pathway Special Warrants”) and the conversion of up to 2,488,417 Series 3 preferred shares (the “Series 3 preferred shares”) to be issued by the Company to holders of the senior notes of the Company’s operating subsidiary, Axxent Corp. (formerly, Optel Communications Corporation), in exchange for warrants that such persons hold to purchase 2,488,417 common shares of Axxent Corp. No additional cash proceeds will be received by the Company upon the exercise of the Special Warrants or the Pathway Special Warrants. Each Series 3 preferred share will be convertible into one Class B non-voting share upon payment by the holder of \$0.03 per share.
Special Warrants:	An aggregate of 10,000,000 Special Warrants were issued by the Company on March 28, 2000. The Special Warrants were issued at a price of \$18.00 per Special Warrant pursuant to an indenture between the Company and CIBC Mellon, as special warrant agent. Each Special Warrant entitles the holder to receive, without payment of additional consideration, one Class B non-voting share (subject to adjustment in certain events) until the date (the “Expiry Date”) that is the earlier of: (i) the sixth business day after a receipt is issued in the province in which the purchaser of Special Warrants resides (each a “Qualifying Province” and collectively, the “Qualifying Provinces”) for the (final) prospectus (“Final Prospectus”) qualifying the issuance of the Class B non-voting shares to be issued upon exercise of the Special Warrants; and (ii) 4:59 p.m. (Toronto time) on March 28, 2001. Any Special Warrants not exercised on or before 5:00 p.m. (Toronto time) on the Expiry Date shall be deemed to have been automatically exercised by CIBC Mellon on behalf of the holder at that time. See “Private Placement and Plan of Distribution”.
Qualification Condition:	If a receipt for the Final Prospectus has not been issued by the securities regulatory authorities in each of the Qualifying Provinces on or before 5:00 p.m. (Toronto time) on July 31, 2000, the holders of Special Warrants will be entitled, upon exercise, to receive 1.03 Class B non-voting shares for each Special Warrant held without payment of additional consideration.
Use of Proceeds:	The net cash proceeds from the issue and sale of the Special Warrants was \$170,494,992 after deducting the Underwriters’ fees and the estimated expenses of the Special Warrant offering. The Company has or intends to use the net proceeds to finance the planned deployment and further development of its network, potential acquisitions and for other general corporate purposes, including to fund operating losses. See “Use of Proceeds”.
Preferred Shares:	An aggregate of up to 2,488,417 Series 3 preferred shares will be issued by the Company in exchange for an aggregate of up to 7,465,250 previously issued warrants (the “Note Warrants”) of the Company’s operating subsidiary Axxent Corp. upon payment of the applicable Series 3 preferred share conversion price which shall be held by the Company in trust until such Series 3 preferred

shares are converted in accordance with their terms. The holders of the Series 3 preferred shares will have the right to convert each Series 3 preferred share into one Class B non-voting share (subject to adjustment in certain events) upon payment of \$0.03 per share. Upon the issuance of a receipt for the Final Prospectus qualifying the issuance of the Class B non-voting shares issuable upon conversion of the Series 3 preferred shares, the rights of the holders of the Series 3 preferred shares to convert their Series 3 preferred shares will be deemed to have been fully exercised and the registered holders of the Series 3 preferred shares will be deemed to have become holders of Class B non-voting shares. See “Description of Share Capital” and “Description of Certain Indebtedness of the Company”.

Pathway Special Warrants:

An aggregate of 33,333 Pathway Special Warrants were issued as partial consideration in connection with the acquisition by Axxent Corp. of all of the issued and outstanding shares of 1108108 Ontario Inc. which was carrying on business as Pathway Communications. See “Business of the Company – Acquisitions”.

Coattail Provisions:

Holders of Class B non-voting shares of the Company are entitled to the benefit of “coattail provisions” that will give such holders specified rights in the event that a take-over bid meeting certain criteria is made for the Class A voting shares of the Company. See “Description of Share Capital – Coattail Provisions”.

Dividend Policy:

To date, the Company has not paid any dividends to its shareholders. The Company intends to retain its earnings and does not currently expect to pay cash dividends. See “Dividend Policy”.

Risk Factors:

Prospective investors should carefully consider certain risks involved in an investment in the Class B non-voting shares, including, but not limited to: the Company’s limited operating history; the Company’s negative cash flows and losses; the Company’s substantial level of indebtedness; the Company’s ability to obtain additional capital; the variability of operating results; the Company’s failure to implement its business plan; the Company’s limited experience operating as a CLEC; the rapid technological changes in the telecommunications industry; increases in customer attrition rates; the failure to migrate customers to Axxent Inc.’s switches; the failure of the Company’s information systems; the reliability of the networks, services and equipment of third party providers; the dependence of the Company on facilities leased or purchased from the ILECs; Year 2000 compliance; the availability and condition of local copper lines; the possibility of interference or claims of interference of DSL technology with other transport technologies on the local copper line; the lack of voting rights of the Class B non-voting shares; the influence of executive officers, directors and principal shareholders in respect of any matter requiring shareholder approval; the restrictions on foreign ownership of the Company under the *Telecommunications Act* (Canada); the immediate dilution to be suffered by holders of Class B non-voting shares; the volatility of the market price of the Class B non-voting shares; the significant levels of government regulation; changes in the value of the Canadian dollar; the ability of the Company’s subsidiaries to pay dividends to fund the Company’s cash requirements; the terms of the Company’s present and future indebtedness; the absence of cash dividends; the Company’s dependence on certain key personnel; the high degree of competitiveness in the telecommunications industry; the successful completion and integration of

acquisitions; and the accuracy of forward looking statements. See “Risk Factors”.

Summary Financial and Other Data

The summary of the Company's historical consolidated financial and other data set forth below as of September 30, 1997, 1998 and 1999 has been derived from the audited consolidated financial statements appearing elsewhere in this prospectus. The summary of the Company's historical consolidated financial and other data set forth below for the six months ended March 31, 1999 and 2000 has been derived from the Company's unaudited consolidated financial statements which include all adjustments that management considers necessary for a fair presentation of the financial position and results of operations for those periods. Operating results for the six months ended March 31, 1999 and 2000 are not necessarily indicative of the results that may be expected for the entire year. The information set forth below should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations – Results of Operations" included elsewhere in this prospectus.

	<u>Year Ended September 30,</u>			<u>Six Months Ended March 31,</u>	
	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>1999</u>	<u>2000</u>
				(unaudited)	
	(dollars in thousands, except per share amounts and operating data)				
Statement of Operations Data:					
Revenue	\$ 12,975	\$ 31,694	\$ 45,860	\$ 21,308	\$ 29,852
Expenses:					
Cost of services	10,015	23,552	33,901	15,591	22,504
Selling, general and administrative	6,702	14,173	27,225	9,355	28,322
Depreciation and amortization	<u>653</u>	<u>1,874</u>	<u>3,967</u>	<u>1,163</u>	<u>5,590</u>
Loss before undernoted	(4,395)	(7,905)	(19,233)	(4,801)	(26,564)
Other income (expenses):					
Interest income	—	1,263	1,521	629	2,008
Interest expense	(569)	(6,464)	(8,396)	(3,928)	(4,670)
Financing expenses ⁽¹⁾	0	(3,716)	(834)	—	—
Foreign exchange gain (loss)	<u>—</u>	<u>(76)</u>	<u>(307)</u>	<u>(139)</u>	<u>127</u>
Net loss	<u>\$ (4,964)</u>	<u>\$ (16,898)</u>	<u>\$ (27,249)</u>	<u>\$ (8,239)</u>	<u>\$ (29,099)</u>
Loss per share – basic	(0.76)	(1.79)	(2.88)	(0.87)	(1.36)
Weighted average Class A voting and Class B non-voting shares outstanding	6,543,866	9,441,556	9,471,012	9,467,142	21,380,956
Other Financial Data:					
Capital expenditures	1,122	1,667	21,086	721	44,290
EBITDA ⁽²⁾	(3,742)	(6,031)	(15,266)	(3,638)	(20,974)
Ratio of earnings to fixed charges ⁽³⁾	—	—	—	—	—
Operating Data (at end of period):					
Total access lines in service	25,838	52,848	71,939	65,075	105,918
On-net access lines in service	0	0	58	0	9,038
Total business customers	8,022	11,622	17,646	13,261	25,546
Number of employees	162	208	452	234	642
	<u>As of September 30,</u>			<u>As of March 31,</u>	
	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>1999</u>	<u>2000</u>
				(unaudited)	
Balance Sheet Data:					
Cash and cash equivalents	\$ 114	\$ 27,277	\$ 21,392	\$ 21,646	\$ 208,868
Capital assets, net	867	2,306	28,557	2,721	71,527
Total assets	7,270	40,692	76,465	36,868	339,966
Total debt, including capital leases	5,170	53,403	61,770	57,035	66,069
Shareholders' equity (deficit)	(1,968)	(18,857)	(9,733)	(27,094)	250,710

(1) Financing expenses relate to the costs associated with the issuance of the 1997 Notes on December 31, 1997 and the costs associated with the April 1999 consent solicitation to modify the 1997 Notes. See "Description of Certain Indebtedness". These costs were expensed when incurred.

(2) Earnings before interest, taxes, depreciation and amortization ("EBITDA") consists of net loss before interest, income taxes, depreciation and amortization, financing expenses and foreign exchange gain (loss). It is a measure commonly used in the telecommunications industry and is presented to assist in understanding Axxent Inc.'s operating results. However, it is not intended to represent cash flow or results of operations in accordance with Canadian generally accepted accounting principles ("GAAP").

- (3) Earnings were inadequate to cover fixed charges and accordingly the deficiency of earnings available to cover fixed charges is \$4,307, \$10,015, \$18,010, \$4,007 and \$23,693 for the years ended September 30, 1997, 1998, 1999 and the six months ended March 31, 1999 and 2000, respectively. For the purposes of calculating the deficiency of earnings available to cover fixed charges, earnings consist of net loss for the period adjusted for the exclusion of fixed charges. Included in fixed charges are interest on long-term debt, amortization of U.S. hedge costs, preferred stock dividend requirements and the interest component of rental expense.

THE COMPANY

Axxent Inc. (formerly, OCI Communications Inc.) (the “Company”) was incorporated under the *Business Corporations Act* (Ontario) (the “*Business Corporations Act*”) on February 2, 1999 as an Ontario numbered company to own all of the issued and outstanding shares of Optel Communications Corporation. On April 1, 1999, the Company completed the reorganization that gave effect to this holding company/operating company structure. By articles of amendment dated April 1, 1999, the Company changed its name to Optel Communications Inc. and created the Class A voting shares and Class B non-voting shares. The articles of incorporation, as amended, of the Company are hereinafter referred to as the “Articles”.

By articles of amendment dated September 16, 1999, the Company changed its name from Optel Communications Inc. to OCI Communications Inc. The Company filed articles of amalgamation on October 1, 1999 to amalgamate four companies that it has recently acquired, Canadian Telecom Resellers Association Inc. (“CTRA”), 1108108 Ontario Inc., operating as Pathway Communications (“Pathway”), Oakbrook Communications Inc. and Interpath Technologies Inc. into the Company’s operating subsidiary, Axxent Corp. See “Business of the Company – Acquisitions” and “Description of Share Capital”.

In connection with a capital reorganization completed on October 27, 1999, the Company effected a consolidation of all of its outstanding Class A voting shares, Class B non-voting shares and options to purchase Class B non-voting shares on a three-for-one basis. See “Capital Reorganization”.

By articles of amendment dated May 29, 2000, the Company changed its name from OCI Communications Inc. to Axxent Inc.

The Company’s operating subsidiary was incorporated on October 26, 1994 under the *Business Corporations Act* and has met all of the requirements of the Canadian Radio-television and Telecommunications Commission (the “CRTC”) to operate as a competitive local exchange carrier (“CLEC”) in Canada. By articles of amendment dated June 1, 2000 the Company’s operating subsidiary changed its name from Optel Communications Corporation to Axxent Corp.

INDUSTRY BACKGROUND

Prior to 1990, telecommunications markets in Canada were divided into geographic regions, with one incumbent local exchange carrier (“ILEC”) having a monopoly for local and long distance telecommunications services in each such region. ILEC monopolies covering the local and long distance markets were first affected by a 1990 CRTC decision to allow limited resale of long distance services in Canada and later by a 1992 CRTC decision to allow unlimited resale and facilities-based competition in the long distance market. Similar to the CRTC’s 1992 decision regarding facilities-based competition in the long distance market, the CRTC’s May 1, 1997 decision (the “Local Competition Decision”) has opened Canada’s local telecommunications services market to switch-based competition effective January 1998. Currently, the ILECs include such companies as Bell Canada and TELUS Communications Inc.

The telecommunications market in Canada is continuing to grow at a robust rate. Lemay-Yates Associates Inc. (“Lemay-Yates”), a telecommunications consulting firm located in Montreal, Quebec, estimates that total business telecommunications revenue grew from \$9.7 billion in 1996 to \$11.7 billion in 1999, representing a compounded annual growth rate of approximately 6.8%. This compares to all average economic growth of approximately 3%. Also, according to Lemay-Yates, telecommunications revenues attributable to the business data services market in Canada, including revenue from Internet services net of carrier costs, are estimated to have grown from \$1.8 billion in 1996 to \$3.9 billion in 1999, representing a compounded annual growth rate of 29%.

Local Services

Local exchange carriers (“LECs”) provide connections for local voice and data calls such as telephone calls or connections to Internet service providers (“ISPs”). LECs generate revenue by providing local service to their customers and from long distance providers who pay access charges to complete long distance voice and data calls in the local

exchange carrier's area. Certain LECs also provide long distance services to their customers.

The local services market consists of:

- *Switched Services:* A service providing dialtone for local calls from one end-user to another. These services include individual telephone lines, Centrex and switched data lines, private branch exchange ("PBX") trunks and optional services such as call waiting, call forwarding, call display and voicemail. PBX is a switching system within an office building which allows calls from outside to be routed directly to the individual instead of through a central exchange. Centrex is a service similar to that of a PBX except that the necessary equipment is located at a network service provider's central office rather than the customer's premises.
- *Private Line Services including Data Transmission:* Dedicated private lines are circuits that have their starting and ending points in the same local area. For data transmission, a private line provides a continuous connection between two end-users. Other forms of data transmission include packet and cell-based technologies which can connect point-to-point or multi-point networks. For voice transmissions, dedicated private lines are used in instances where usage is very high between end-user locations.
- *Switched Access to Long Distance Services:* This service provides access for traditional long distance calls which allow end-users to connect to long distance providers of their choice on demand, such as when a customer dials 1+.
- *Dedicated Access Services:* Dedicated access services bypass the ILEC local switched network to connect end-users to long distance voice and data networks. Dedicated access is typically provided by using local private line services.

Long Distance Services

Long distance providers connect local networks for voice and data transmission. Data and voice transmissions originating from one end-user travel over a local network to the long distance provider's point-of-presence (the "POP"), which is the location of the network equipment. Here, the transmissions are combined with other transmissions and sent to another POP before being routed to another local network for transmission to a different end-user.

Long distance providers (such as the ILECs and other competitive long distance providers) generate revenue from outbound long distance calls as well as inbound toll free services such as 1-800 calls.

Data and Internet Services

The Internet has quickly emerged as a dominant service in both the business and residential markets, with growth rates that are expected to dramatically outpace the growth rates for voice services. Current offerings include a wide array of dedicated and switched data services such as:

- *Dial-Up Internet Access services:* Such services allow users to access the Internet through a modem.
- *ISDN Services:* Integrated services digital network ("ISDN") services provide end-to-end digital connectivity for simultaneous transmission of voice and data on internationally-defined standards and are used to access an Internet connection.
- *Frame Relay Services:* Frame relay is a high-speed data service for switched data communications between computers. Frame relay supports speeds from 56 thousand bits per second to the T-1 rate.
- *FDDI Services:* Fibre distributed data interface ("FDDI") is used in connection with optical-fibre based token-ring networks and features dual counter-rotating rings, each with a data transmission capacity

of 100 million bits per second. FDDI provides for reliable data transfer, active link monitoring and station managing.

- *ATM Services:* Asynchronous transfer mode (“ATM”) is a high-speed multiplexing and switching method utilizing fixed-length packets to support multiple types of data traffic.

Data and Internet services are primarily provided by:

- LECs that offer Internet and data services;
- independent ISPs that provide local Internet access to residential and business subscribers;
- long distance providers that offer dedicated data transmission services between local networks;
- cable companies who are increasing their penetration of the residential market by offering access services over their existing cable plant; and
- multi-channel multi-point distribution service (“MMDS”, also known as “wireless cable”) providers such as Look Communications Inc.

Emergence of DSL Technology

Digital subscriber line (“DSL”) technology allows multiple forms of data, voice and video to be carried over copper wire on the local loop between a network service provider’s central office and the customer site. DSL technology is expected to have a significant impact on the telecommunications market in the near future by supporting high-speed Internet and intranet access, online services, interactive entertainment and voice transmission to business, small office, home office and consumer markets. The major advantage of DSL services is that they can be supported on ordinary copper telephone lines connected to most commercial and residential buildings.

DSL technology emerged in the early 1990s and is commercially available today to address the performance bottlenecks of the public switched telephone network. DSL equipment, when deployed at each end of standard copper telephone lines, increases the data carrying capacity of these lines by up to 100 times depending on the length and condition of the local loop. In addition, DSL technology can be used in voice applications to carry up to 24 voice lines simultaneously on a single local loop, which provides significant opportunity for margin improvement. Digital signal processing coupled with falling equipment prices has made the deployment of DSL technology on a widespread basis more economical.

Because DSL technology uses the existing copper telephone lines and can carry up to 24 voice lines simultaneously on a single local loop, it is significantly less expensive to deploy on a broader scale than other high-speed digital communication technologies, such as fibre-based voice networks, cable modems, wireless data and satellite data. A significant portion of the investment in a DSL network can occur once the customer has been successfully acquired. As a result, such networks require a comparatively lower initial fixed investment, and the subsequent variable investments in DSL equipment are directly related to the number of paying customers.

BUSINESS OF THE COMPANY

Overview

Axxent Inc. is a rapidly growing Canadian telecommunications provider of voice, data and Internet services. The Company targets small and medium-sized businesses, a sector that management believes to be under-served by the large telephone companies and that management believes has significant revenue and profit potential.

In order to facilitate its entrance into the telecommunications market as early as possible, the Company began operations as a reseller of local telephone services in January 1995. Management believes this was the best way to enter the market as it enabled the Company to establish a customer base in order to capitalize on the lowering of unbundled local loop rates and the commencement of facilities-based competition in January 1998. As of April 30, 2000, Axxent Inc. had over 105,000 access lines in service and in excess of 25,000 customers.

The Company is one of 15 CLECs that have met all of the requirements of the CRTC to operate as a CLEC in Canada and was one of the first CLECs to co-locate in the principal metropolitan centres of Toronto and Montreal. Axxent Inc. operates its own switching equipment in the Company's head office in Toronto as well as in the Company's Montreal office. Axxent Inc. has purchased, installed and is utilizing DMS-500 switching equipment purchased from Nortel Network Corporation ("Nortel") to provide its voice services and ATM switches purchased from Cisco Systems Inc. ("Cisco Systems") for its data services. The Company intends to offer facilities-based voice and data services in Canada's major markets outside of Toronto and Montreal, including Vancouver, Calgary, Quebec City, Ottawa-Hull, Kitchener-Waterloo, London, Barrie and Hamilton. The Company's business plan calls for Axxent Inc. to have established co-location sites in 100 incumbent local exchange carrier ("ILEC") central offices in those markets by the end of fiscal 2000.

The Company has grown rapidly. Revenues have increased from \$1.4 million for the fiscal year ended September 30, 1996 to \$45.9 million in fiscal year 1999. For the six months ended March 31, 2000, Axxent Inc.'s revenues were \$29.9 million compared to \$21.3 million for the same period in the prior fiscal year.

The Company intends to provide its customers with a comprehensive bundle of enhanced voice, data and Internet services. Although most of the Company's current revenue is from voice-related services, management believes there are significant growth opportunities in providing Internet access and high-speed data services to its customers. Management believes the Company will be one of the first Canadian CLEC to offer high-speed data services using DSL technology. To capitalize on these opportunities, Axxent Inc. acquired Pathway and EDI Communications Networking Inc. ("EDI Communications"). The Company has also been granted Cisco Powered Network status.

Axxent Inc. entered into an agreement dated as of January 1, 2000 to form a joint venture with Rhythms NetConnections, Inc. ("Rhythms NetConnections"), one of the leading providers of DSL-based services in the United States. Pursuant to the agreement, the parties established Rhythms Canada Inc. ("Rhythms Canada"), a New Brunswick company which was incorporated on December 31, 1999. Rhythms Canada allows the Company to focus on its target small to medium-sized business customers for DSL-based services while transferring its high-speed data services and wholesale customers to Rhythms Canada. Axxent Inc. has agreed to use Rhythms Canada products and services when marketing DSL-based data services to small and medium-sized businesses. The Company has structured the joint venture so that Axxent Inc., and not Rhythms Canada, has the right to market DSL-based data services to small and medium-sized business customers as well as certain specified large business customers while Rhythms Canada, through its own sales force, offers dedicated high-speed DSL-based services to large and wholesale customers, including ISPs, carriers and value-added resellers.

Network Design

The Company's network design is based on the use of DSL technology and its network deployment strategy is what is commonly referred to in the telecommunications industry as a "smart build strategy".

When deployed, DSL equipment increases the data-carrying capacity of a standard copper telephone line (a

“local loop”) by up to 100 times. In addition, DSL-based technology can be used in voice applications to carry up to 24 voice lines simultaneously on a local loop, which management believes provides significant opportunity for efficiencies and margin improvement.

Using the Company’s smart build strategy, the Company will own only the strategic assets in its network, such as switches and customer premises equipment. This is in contrast to a traditional “fibre build strategy” where a carrier builds and owns most, if not all, the assets in its network. The use of a smart build strategy requires less capital than a fibre build strategy, offers attractive gross margins, minimizes time to market and facilitates capital efficiency. See “– Business Strategy”.

Market Opportunity

There are a number of factors that exist in the Canadian telecommunications market that create a particularly attractive opportunity for a CLEC. Management believes these factors include the following:

Large Market Opportunity

The telecommunications market in Canada is continuing to grow at a robust rate. Lemay-Yates estimates that Canada’s telecommunications services industry revenue, including local, long distance data and Internet service was approximately \$17.8 billion in 1999, with business services accounting for approximately 65% of this total. The following table demonstrates the Lemay-Yates published estimates for revenue growth in this market:

Total Canadian Telecommunications Market Revenue Forecast by Service (in millions of dollars)

Service	1999	2004	Compound Annual Growth Rate (%)
Data	\$ 3,429	\$ 7,740	17.7%
Internet	476	1,222	20.8%
Long Distance	3,788	3,282	(2.8%)
Total Residential	6,102	7,191	<u>3.3%</u>
Business Local Voice	<u>3,993</u>	<u>4,575</u>	<u>2.8%</u>
Total	<u><u>17,788</u></u>	<u><u>24,010</u></u>	<u><u>6.2%</u></u>

High-Growth Data Services Opportunity

Management believes that the growing demand for high-speed digital communications bandwidth has created a substantial market opportunity. High-speed Internet access has become important to small and medium-sized businesses due to the emergence of electronic commerce (“e-commerce”) as businesses establish their web sites and corporate intranets and extranets to expand their customer reach and improve their communications efficiency. According to International Data Corporation (“IDC”), 23% of Canadians or approximately 6.9 million people used the Internet in 1998, and this number is forecasted to grow to approximately 19.2 million people or 64% of Canadians by 2003. Accordingly, to remain competitive, small and medium-sized businesses increasingly need high-speed Internet connections to maintain complex web sites, access critical business information and communicate with employees, customers and business partners more efficiently. Management believes that the Company is well positioned to capitalize on the high-growth data services opportunities through its acquisition of Pathway, the establishment of Rhythms Canada, Axxent Inc.’s use of DSL-based technology and the Company’s equipment purchase and joint marketing agreement with Cisco Systems.

Favourable Regulatory Environment for Canadian owned CLECs

There are a number of aspects of the Canadian regulatory environment which create a favourable climate for growth. These are:

- *Single National Regulator.* The CRTC has jurisdiction over all telecommunications services provided by Canadian carriers, including ILECs, CLECs, wireless providers and competitive long distance providers. This structure reduces the possibility of jurisdictional disputes relating to telecommunications regulation between the federal and provincial levels of government.
- *The May 1997 CRTC Decision to Deregulate Local Services.* The Local Competition Decision opened Canada's local telecommunications market to facilities-based competition effective January 1, 1998. Management believes that this decision created a favourable regulatory framework that will allow the CLECs to capture market share from the ILECs.
- *Reduction in Unbundled Local Loop Rates.* In December 1998, the CRTC significantly reduced the tariffed rates proposed by the ILECs for permitting the CLECs to use the ILECs' unbundled local loops. This decision further enhanced the attractiveness of the Company's smart build strategy in comparison to alternative network deployment strategies.
- *Flexibility in Pricing and Bundling of Services.* CLECs are currently subject to a lesser degree of regulation than the ILECs, giving them more flexibility in the services they offer and the prices they can charge for these services. In contrast, the ILECs are required to obtain the approval of the CRTC for changes to pricing or the bundling of certain services.

Business Strategy

The Company's goal is to become the telecommunications provider of choice for small and medium-sized businesses in Canada by offering bundled voice, data and Internet services. Deployment of data capabilities in the Company's network has begun with the initial establishment of a DSL-based high-speed access network through Rhythms Canada and the establishment of co-location sites in Canada by the Company. Axxent Inc. plans to grow this network rapidly.

The key elements of the Company's business strategy include the following:

Capitalize on Favourable Economics of Smart Build Strategy Using DSL Technology

DSL technology allows the Company to significantly improve its overall margins by carrying up to 24 voice lines simultaneously over a single local loop and increasing data-carrying capacity and enabling the Company to deliver multiple voice telephone lines to a customer over a single local loop. In addition, the Company's smart build strategy requires much less capital than would a fibre build strategy and facilitates capital efficiency, because much of the capital is deployed only after Axxent Inc. contracts with a customer.

Provide Integrated Services With a New Emphasis on Data

The rapid growth of the Internet, expansion of e-commerce and the introduction of new business applications have fuelled increasing demand in the Company's target market for access to high-speed data services. To help meet these needs, the Company formed Rhythms Canada with Rhythms NetConnections to establish a nationwide dedicated high-speed data network. In addition, the Company has signed a preliminary marketing agreement with Research in Motion Limited ("RIM") pursuant to which the Company will distribute RIM's BlackBerry™ Internet Edition ("BBIE") in Canada. The Company will offer its customers a single-mailbox, wireless Internet solution that will allow Axxent Inc.'s customers to access their e-mail through a BlackBerry Wireless handheld device and through a personal computer.

Axxent Inc. intends to market data services to its small and medium-sized business market. To implement the Company's data strategy, Axxent Inc. has acquired Pathway and EDI Communications and will be using equipment purchased from Cisco Systems, Paradigm Communications Group and Copper Mountain Networks, Inc. to provide DSL-based data and other Internet services. The Company is a single source provider of bundled telecommunications services, offering voice, data and Internet services. See "– Service Offerings".

Target Under-Served Small and Medium-Sized Business Market

Customers in the Company's targeted small and medium-sized business market typically purchase telecommunications services from multiple vendors and do not have dedicated personnel with telecommunications expertise. The Company's business plan calls for it to further grow its base of co-location sites to 100 by the end of fiscal 2000, which management believes will provide the Company with the ability to access markets with approximately 4.0 million business access lines in principal business centres across Canada.

Leverage Axxent Inc.'s Early to Market Advantage

In order to facilitate the Company's entrance into the telecommunications market as early as possible, Axxent Inc. began its operations as a reseller of local voice services in January 1995. As of April 30, 2000, the Company had over 105,000 access lines in service and in excess of 25,000 customers. The Company's early entry into the telecommunications market has afforded it many advantages, including the following:

- Axxent Inc. is one of 15 CLECs that are qualified to operate in Canada and was one of the first CLECs to co-locate in the principal metropolitan centres of Toronto and Montreal. The Company is planning to establish 100 co-locations sites in Ontario, Quebec, Alberta and British Columbia by the end of fiscal 2000. As at May 5, 2000, the Company had 117 co-location sites in process and had two data and two voice switches as well as 35 co-location sites in service at such date.
- The Company expects there to be high demand from ISPs and other enterprise customers for high-speed data services being provided by Rhythms Canada due to the high rates charged by the ILECs to provide high-speed data access to the ISPs.
- Management believes that Axxent Inc. is one of the first Canadian CLECs to offer high-speed data services using DSL-based technology and will market the Company's DSL-based data services to its small and medium-sized business target market.
- The Company has an established and well-trained in-house sales force of approximately 80 representatives. In addition, Axxent Inc. has recently acquired Optimum Teleservices Inc. ("Optimum Teleservices"), a telemarketing sales company. The Company uses Optimum Teleservices to target customers who have less than 10 lines. Optimum Teleservices adds approximately 120 additional representatives who sell the Company's telecommunications services through telemarketing and other sales channels.

Continue to Provide Superior Customer Services

Through a commitment to customer service and innovative pricing and term contracts, Axxent Inc. has achieved customer loyalty and historically low customer attrition rates. The Company utilizes a centralized team of highly trained customer sales and service representatives to co-ordinate initial inquiries and handle any post-installation billing and customer care issues. A dedicated team is used to retain existing customers, to ensure their satisfaction and to offer new products and services. Management believes that the Company's continued focus and efforts on satisfying its customers will help it retain and attract customers.

Leverage Sophisticated Back Office Systems

The Company has implemented and is in the process of integrating a scalable operational support system that allows for the rapid provisioning of service, the highest level of customer support and accurate and timely billing. Axxent Inc. selected MetaSolv Software Inc. ("Metasolv"), In-Logic Software Inc. ("In-Logic") and Saville Systems Canada, Ltd. ("Saville Systems") as its operational support software vendors. As a result of this process, which management believes is the first of its kind in Canada, Axxent Inc. expects to gain a more efficient and streamlined customer service process. One of the key elements to the Company's system will be the ability of its customers to pay their bills, update account status and subscribe to new services over the Internet. Management believes that these

systems will provide Axxent Inc. with a competitive advantage by allowing the Company to process orders effectively and to provide outstanding customer service. This system is being integrated with trouble ticket management, customer service, inventory, billing and collection services as well as the Company's customer retention and upsell marketing efforts. Existing systems deployed by most ILECs and long distance providers require multiple entry of customer information to accomplish order management, switch administration and billing. Management believes that it is important to have an integrated system with a single point of data entry in order to reduce labour costs and customer service errors. Management further believes that the integration of these systems will enhance the Company's competitive advantage by allowing Axxent Inc. to scale its business rapidly through the addition of customers while minimizing human intervention and the possibility of error which will permit the Company to process orders effectively and to provide outstanding customer service.

Continue to Pursue Acquisitions and Strategic Alliances.

The pursuit of growth opportunities and strategic acquisitions of telecommunications companies in Canada is an element of the Company's business strategy. Acquisition opportunities will be considered by Axxent Inc. where the target has a technology, customer base or business complimentary to that of the Company.

Utilize the Experience of the Company's Management Team

The Company has built a strong management team with extensive experience in the Canadian telecommunications industry. Members of the senior management team have an average of 19 years' experience in the telecommunications industry and have held key executive and operating positions in start-up and well established telecommunications companies in Canada, including Bell Canada, AT&T Canada Inc. (MetroNet) ("AT&T Canada"), Rogers Cantel Inc. and Call-Net Enterprises Inc. ("Call-Net"). The management team is led by Robert Latham, the Company's President and Chief Executive Officer, who has over 30 years experience in the telecommunications industry.

Rhythms Canada Joint Venture

Strategic Considerations. As of January 1, 2000, the Company entered into a joint venture agreement (the "Rhythms Joint Venture Agreement") with Rhythms NetConnections, a leading U.S. provider of high-speed local access network solutions using DSL-based technology, to establish Rhythms Canada. Axxent Inc. and Rhythms NetConnections own an equal number of the issued and outstanding common shares of Rhythms Canada and have equal representation on the board of directors. By the terms of the Rhythm's Joint Venture Agreement, Rhythms Canada is not permitted to compete directly with Axxent Inc. in the small and medium-sized business market. Rhythms Canada was incorporated under the laws of New Brunswick on December 31, 1999 and is based in Toronto, Ontario. On April 25, 2000, Rhythms Canada announced the launch of its DSL data service in Toronto and Montreal.

There were a number of strategic reasons why Axxent Inc. chose to establish a joint venture with Rhythms NetConnections including:

- to draw upon the expertise of Rhythms NetConnections in establishing a DSL-based data network;
- to reduce the costs and shorten the time necessary to commence operation of the Company's DSL-based data service;
- to access the Rhythms NetConnections brand name and credibility; and
- to firmly establish leadership in the DSL-based data market in Canada.

Structure of the Joint Venture. The Rhythms Joint Venture Agreement provides that Axxent Inc. and Rhythms NetConnections each contributed specified assets and services to Rhythms Canada. The Company has contributed and is continuing to contribute, among other things, its marketing and sales expertise, distribution

agreements and partners, access to third party alliances, management and expert human resources (including technological, legal and regulatory skills), existing customer contracts within the scope of the joint venture, arrangements with suppliers and information systems. Rhythms NetConnections has contributed and is continuing to contribute, among other things, its marketing and sales expertise, distribution agreements and partners, access to third party alliances, management and expert human resources, products, technology, information systems and the Rhythms brand name. In addition, each party has entered into licensing agreements with Rhythms Canada to provide for the availability of improvements of existing technology or new technology developed or acquired by either party which relate to the services to be provided by Rhythms Canada. Rhythms Canada uses the transmission facilities which the Company owns and operates.

The Company has agreed to use Rhythms Canada products and services when marketing DSL-based data services to small and medium-sized businesses. Axxent Inc. is also required to give Rhythms Canada first opportunity to provide DSL-based data products and services to the Company which it, in turn, will provide to the Company's small to medium-sized business customer base. In addition, Rhythms Canada has agreed to utilize the Company's switched services if Rhythms Canada provides DSL-based voice services to its customers. By participating in the Rhythms Canada joint venture, Axxent Inc. expects to leverage the joint venture's focus on selling DSL-based data services to large enterprise and wholesale customers and the Canadian component of the Rhythms NetConnections customer base.

Since Rhythms Canada is not a Canadian owned and controlled corporation, it is prohibited from owning or operating transmission facilities or leasing space in or owning equipment in ILEC offices. However, Rhythms Canada owns all of the DSL network assets beyond the network termination point, including switches and related equipment at the point of presence. Axxent Inc. owns the network assets which Rhythms Canada is prohibited from owning and leases such assets to Rhythms Canada on commercially reasonable terms. Rhythms Canada is managed on a day-to-day basis by a president appointed by a supervisory board made up of an equal number of representatives appointed by each of the Company and Rhythms NetConnections. The supervisory board is responsible for the overall management and supervision of the joint venture.

Under the terms of the Rhythms Joint Venture Agreement, the Company purchased U.S.\$10.0 million of preferred shares of Rhythms Canada. The Rhythms Canada preferred shares earn dividends at a rate of 6% per annum. The Company has the right to cause Rhythms Canada to redeem its preferred shares on:

- the sale by Rhythms NetConnections' of any of its equity holdings in Axxent Inc. on a proportionate basis;
- Rhythms Canada completing an arm's length financing transaction in excess of U.S.\$25.0 million;
- Rhythms Canada becoming "EBITDA positive" as defined in the Rhythms Joint Venture Agreement; or
- Commencing on January 1, 2003, and on each anniversary thereafter, the holders of the Rhythms Canada preferred shares have the right to require Rhythms Canada to repurchase all or any portion of their shares at a price equal to the issue price plus accumulated but unpaid dividends.

In addition to the preferred stock investment of the Company, Axxent Inc. and Rhythms NetConnections each initially purchased U.S.\$100 in voting Class A shares in the capital of Rhythms Canada. Any further funding requirements must be approved by Rhythms Canada's board of directors and are to be provided on a pro rata basis at a price determined by the board.

In December, 1999, the holders of the Company's 1997 Notes (as hereinafter defined) consented to the Company executing the Rhythms Joint Venture Agreement and completing the purchase of U.S. \$100 in voting Class A shares and up to U.S. \$10.0 million of preferred shares in the capital of Rhythms Canada. In May 2000, the holders of the 1997 Notes consented to certain amendments to the securities purchase agreement dated December 31, 1997 under which the 1997 Notes were issued. Under these amendments, the Company is permitted to invest up

to U.S. \$50.0 million, whether by purchase of assets from Rhythms Canada, purchase of Class A shares or preferred shares, capital contribution, loan, advance or guarantee of indebtedness of Rhythms Canada. In addition, the Company will be able to sell or lease assets to Rhythms Canada provided that such transactions are completed at either the direct cost to the Company or on commercially reasonable terms.

In connection with the joint venture negotiations, Rhythms NetConnections purchased a special warrant (the “Rhythms Special Warrant”) of Axxent Inc. for U.S.\$5.3 million. The Company qualified the distribution of the Class B non-voting shares issued upon exercise of the Rhythms Special Warrant under a prospectus dated December 9, 1999. The Rhythms Special Warrant was automatically exercised, for no additional consideration, for 763,680 Class B non-voting shares on December 19, 1999. The Company used the proceeds from the sale of the Rhythms Special Warrant to help fund its capital contributions to the joint venture. See “Prior Sales” and “Description of Share Capital”.

In addition, Rhythms NetConnections has the right to designate one member for election to the Company’s board of directors. Scott Chandler has been appointed to the board as Rhythms’ NetConnections’ representative.

Other Strategic Acquisitions and Alliances

Bell Canada. The Company’s operating subsidiary, Axxent Corp., has recently entered into a supply and service agreement with Bell Canada (“Bell”). The agreement provides Bell with revenue guarantees over the next five years, and gives Axxent Corp. price certainty and service guarantees which will enable the Company to deliver and maintain a very high degree of service quality and reliability. The services to be provided under the agreement include digital, toll, Centrex resale, calling card and 1-800.

Nortel. The Company has entered into an equipment purchase agreement with Nortel which provides for the purchase of \$39.0 million of telecommunications equipment and services.

CTRA. In June 1999, through the acquisition of Oakbrook Communications Inc., the Company’s operating subsidiary acquired CTRA, a start-up wholesale long distance reseller that has negotiated aggressively priced long distance services from long distance carriers which it resells at a mark-up to small long distance resellers.

Pathway. In July 1999, the Company’s operating subsidiary acquired Pathway, an ISP whose Internet service has been ISO 9002 certified. Pathway also offers value-added services such as e-commerce and network integration in addition to its other Internet services. The acquisition of Pathway allows Axxent Inc. to offer expanded bundled voice, Internet and data services to the small and medium-sized business market. See “– Acquisitions”.

RIM. On February 14, 2000, Axxent Inc. signed a preliminary marketing agreement with Research in Motion Limited (“RIM”) pursuant to which the Company’s operating subsidiary will distribute RIM’s BlackBerry™ Internet Edition (“BBIE”) in Canada. The Company will offer its customers a single-mailbox, wireless Internet solution that will allow customers to access their e-mail through a BlackBerry wireless handheld device and through a personal computer. Under the agreement, the parties have agreed to negotiate a supply agreement obligating the Company to purchase no less than 11,000 RIM BBIE handheld products during a term of no more than two years from the date of the definitive supply agreement. RIM will provide the Company with standard customer support services.

EDI Communications. On March 23, 2000, Axxent Inc. completed the acquisition of all the issued and outstanding shares of EDI Communications, an Ontario based company specializing in data network provisioning, including data network design, implementation and operations, for small and medium-sized businesses. As consideration for the transaction, Axxent Inc. issued 210,938 Class B non-voting shares at closing. In addition, Axxent Inc. may be required to issue up to an additional \$5.65 million in Class B non-voting shares if certain performance targets are met. The number of additional shares will be determined using the weighted average closing price of the Company’s Class B non-voting shares for the five trading days prior to the date upon which such shares are issued. Pursuant to a purchase agreement dated June 8, 2000, Axxent Inc. transferred all of the issued and outstanding shares of EDI Communications to Axxent Corp. in exchange for 211,237 common shares of Axxent Corp. See “– Acquisitions”.

Simcoe County. On March 29, 2000 the Company's operating subsidiary completed the acquisition of all of the issued and outstanding shares of Simcoe County Long Distance Corporation ("Simcoe County") and Quinte Long Distance Corporation ("Quinte Long Distance"). These organizations had a combined customer base of approximately 1,800 local business customers comprising more than 10,000 business lines, annual revenues of approximately \$9.0 million and a proven history of positive earnings. The purchase price of the acquisition was \$15,000,000 in cash, subject to certain adjustments. Simcoe County is the largest alternate provider of business local and telecommunication services in the Barrie, Ontario area and, through its affiliate, Quinte Long Distance, provides similar services to the Belleville, Ontario area. See "– Acquisitions".

Optimum Teleservices. On May 4, 2000, the Company's operating subsidiary completed the acquisition of all of the issued and outstanding shares of Optimum Teleservices Inc. Prior to the completion of such acquisition, Optimum Teleservices had been providing the Company with outbound call centre marketing services under an exclusive contract. The purchase price of the acquisition was \$5.4 million, comprised of \$2.7 million in cash and the issuance of 173,188 Class B non-voting shares, subject to adjustment in certain events.

Service Offerings

The Company is a single source provider of bundled telecommunications services, offering voice, data and Internet services. As an early market entry strategy, Axxent Inc. offered local line voice services by reselling ILEC services in each of its markets. While management believes the gross margins from its current resale revenue is attractive, the Company intends to improve upon these margins using its smart-build strategy. As the Company establishes co-location sites, it has begun to migrate customers to its own network. As of April 30, 2000, the Company had 1,516 business customers and 9,038 access lines on its own network.

The Company offers its customers bundled services. Axxent Inc. has a group dedicated to contract renewal and selling additional products to the Company's customers. See "– Sales and Marketing – Direct Sales".

Current and Planned Service Offerings

Local Telephone Services. Axxent Inc.'s local voice services for customers utilizing its leased lines incorporates a pre-packaged bundle of business features that are included in its competitive monthly line rate. These features include call forwarding, call waiting, three-way calling and call display. The Company's local line service provides a two-way connection between the customer's office and the public switched telephone network. Customers can connect Axxent Inc. lines to telephones, fax machines, modems or multi-line phone systems. The Company also offers voice messaging which provides the customer with the ability to retrieve, reply, send and broadcast messages from any telephone. Customers have the choice of monthly, one-year, two-year and three-year contracts with a discount structure designed to promote long-term contracts.

Long Distance Telephone Services. The Company is an inter-exchange carrier ("IXC"), which allows Axxent Inc. to carry long distance traffic and provide long distance services directly to the Company's current and future customers on the Company's own network. The Company resells domestic and international long distance services. Axxent Inc. launched its long distance service in March 1996, at which time management believes the Company was the first competitive telecommunications service company in Canada other than the ILECs to provide consolidated billing of local and long distance services. The Company's long distance plan includes comprehensive features, such as multiple account codes, customized call summaries and customized reporting. Axxent Inc. also offers customers a calling card service with access to more than 130 countries.

High-Speed Data Services. The Company offers, directly and through Rhythms Canada, a wide array of dedicated high-speed digital data services at speeds of up to 10 million bits per second which will allow businesses to connect data, video and voice networks, establish private networks across office locations and integrate traffic over highly secure networks. Axxent Inc.'s dedicated services now include or are expected to include:

Current Offerings

- xDSL data services
- ISDN
- frame relay
- ATM products which allow for high-speed switching and support multiple types of traffic

Future Offerings

- Internet protocol/virtual private network
- fibre distributed data interface

Internet Services. The Internet services provided by the Company's Pathway Internet division include:

- dial-up Internet access through low cost entry level packages;
- connect-on-demand ISDN Internet service at 64 and 128 thousand bits per second;
- dedicated, high-speed, ISDN, ADSL and T-1 based Internet access; and
- secure, climate-controlled server facilities where the Company locates, manages and maintains Internet servers for companies which need cost effective Internet access.

Each of the Company's Internet products has been designed, packaged and competitively priced based on current and projected market demand. The Company's connect-on-demand service, for example, is an innovative product which allows customers to receive abundant Internet access at prices which are less than those charged by many ISPs for dedicated services.

Network and E-Commerce Services. By offering the Company's business customers the convenience of e-commerce and network services bundled with Internet access in a single package, the Company expects to create stronger, long-term relationships. The Company offers the following network and e-commerce services through our Pathway Internet division:

- provision and management of full Internet service to employee desktops;
- local and wide area network installation, optimization and expansion;
- virtual private networks for secure, intra-branch communications;
- database driven intranets and extranets;
- retail e-commerce services such as e-storefronts and catalogs;
- web hosting; and
- secure, real time Internet credit card transaction processing for Internet merchants.

DSL-Based Services to Wholesale and Large Business Customers through Rhythms Canada. Management believes that large Canadian ISPs are currently frustrated by their inability to provide competitive, high-speed DSL-based Internet access due to the high prices currently charged by the ILECs for wholesale DSL-based services. ISPs have shown interest in the DSL-based data services offered by Rhythms Canada as a substitute for T-1 and ISDN services that they may currently be purchasing, or considering purchasing, from the ILECs.

RIM Blackberry Internet Edition. The Company has signed a preliminary marketing agreement with RIM pursuant to which it will distribute RIM's BBIE in Canada. The Company offers its customers a single-mailbox, wireless Internet solution that will allow Axxent Inc.'s customers to access their e-mail through a BlackBerry wireless handheld device and through a personal computer.

Target Markets

The following table presents a summary of the Company's current and proposed markets and services.

	<u>Market</u>		<u>Axxent Inc.</u>					
	<u>Population</u> ⁽¹⁾	<u>Business Lines</u> ⁽²⁾	<u>Local Line Customers</u> ⁽³⁾	<u>Lines</u> ⁽³⁾	<u>Business Internet Customers</u>	<u>Resale Services</u> ⁽⁴⁾	<u>Facilities-based Services</u> ⁽⁴⁾	<u>Current Co-Locates</u> ⁽⁵⁾
Toronto	4,400,000	1,065,667	12,959	67,754	4,978	Yes	Yes	20
Montreal	3,400,000	683,209	3,204	16,976	49	Yes	Yes	15
Ottawa-Hull	1,000,000	270,163	1,205	5,653	—	Yes	2000	—
Quebec City	698,000	194,923	150	821	—	Yes	2000	—
Southern Ontario ⁽⁶⁾ ...	2,200,000	619,285	2,948	14,377	4	Yes	2000	—
Vancouver	1,900,000	416,493	26	141	—	2000	2000	—
Edmonton	892,000	257,720	5	55	—	2000	2000	—
Calgary	832,000	262,779	5	79	—	2000	2000	—
Winnipeg	677,000	149,616	6	34	—	2001	2001	—
Halifax	<u>347,000</u>	<u>112,780</u>	<u>7</u>	<u>28</u>	<u>—</u>	2000	2001	<u>—</u>
Total target markets	16,346,000	4,032,635	20,515	105,918	5,031			35
Total Canada	29,672,000	6,334,955						

(1) Based on 1996 Statistics Canada population of census metropolitan area.

(2) Based on estimates provided by Lemay-Yates of 1999 business lines.

(3) Customers and voice lines in service and in process as of April 30, 2000.

(4) Future dates are target dates for the roll-out of our services in such markets.

(5) Co-location sites in service as of May 5, 2000.

(6) Southern Ontario consists of the Kitchener-Waterloo region and the cities of Hamilton, Sarnia, Windsor, Oshawa, London and St. Catharines-Niagara Falls, Ontario.

Migration of Current Customers

As of April 30, 2000, the Company had over 105,000 access lines in service. With this base of lines, management believes there are favourable economics in establishing a facilities-based network. By utilizing a smart build strategy and with the deployment of DSL-based technology in the Company's network, management believes that the Company can migrate lines from the ILECs to its network switches on a cost effective basis. For the fiscal year ended September 30, 1999, when the Company was exclusively a reseller of local line services, gross margin generated from resale activities resulted from taking advantage of term and volume discounts in the Bell Canada Centrex tariff. As the Company rolls out its network, it will continue to market voice services on a resale basis in areas where the Company's facilities are not available, and migrate customers once on-net service is available.

Management believes that significant economies of scale can be achieved by migrating existing customers to the Company's network switches. By utilizing a combination of the Company's own switches and DSL equipment, Axxent Inc. can take advantage of low-priced local loops to migrate customers with minimal field work.

Axxent Inc. has begun to service existing customers on its own switches in the most highly populated areas and to grow the Company's network through co-locating with the ILECs.

Sales and Marketing

The Company sells its products and services to its customers through its own direct sales channels, which includes traditional sales and telemarketing, as well as through an indirect agent channel. The Company's traditional sales force is comprised of approximately 80 representatives, and its telemarketing sales force is comprised of approximately 120 representatives. In addition, the Company utilizes a number of other agents and representatives to sell its services.

The Company's traditional sales force focuses primarily on small to medium-sized customers that have a need for greater than 10 lines. Management believes the potential revenue from these types of customers justifies the higher cost of the traditional sales model. On May 4, 2000, the Company completed the acquisition of Optimum Teleservices, a telemarketing sales company which targets customers who have less than 10 lines and who generally can only be cost-efficiently acquired by telemarketing. The Company's overall sales and marketing efforts are managed by the two principals of KEDA Consulting Corp. who are serving roles as Axxent Inc.'s senior vice president, marketing and senior vice president, customer operations. See "Management – Directors, Executive Officer and Key Consultants".

Direct Sales

The Company has segmented its direct sales force into five groups according to customer needs and size.

- *Business Sales.* The business sales group serves customers who require a full range of telecommunications services and use greater than 10 lines. Axxent Inc. staffs this group with experienced salespeople who have a background and proficiency in direct selling. The Company currently has 25 business sales representatives.
- *Major Accounts.* The Company's major accounts sales force deals with customers who have more than 50 lines and have a profile suited to the services Axxent Inc. offers. This group includes companies with multiple locations effectively operating as independent small businesses. The Company currently has 8 major account sales representatives.
- *Data / Internet Sales.* The Company currently sells its business Internet and data products through the direct sales groups of acquired companies, Pathway and EDI Communications. There are currently 22 such sales people.
- *Retention/Upsell Sales.* The Company's retention/upsell sales force focuses on the renewal of existing Axxent Inc. customer contracts before they expire as well as selling additional products and services to the Company's existing customer base. The Company currently has 25 salespeople working in this capacity.
- *Telemarketing.* Axxent Inc. appointed Optimum Teleservices as the Company's hybrid sales channel in July 1999. Optimum Teleservices is managed by experienced telecommunications professionals who have been very successful in selling product lines similar to Axxent Inc. On May 4, 2000, the Company completed the acquisition of Optimum Teleservices adding approximately 120 representatives in Toronto and Montreal who sell Axxent Inc. products and services.

The sales compensation structure varies by sales channel. Direct sales representatives have a comparatively modest base salary and are heavily incented through performance-based compensation. The bonus payment structure for the Company's direct sales representatives provides for bonus payments of up to 75% of their base salary. Sales achievements exceeding performance targets and longer contract terms have additional built in bonus accelerators.

Wholesale Segment

Historically, the Company has concentrated on sales to end users. However, the Company has recently begun selling to the wholesale segment of the market. Management believes that by developing a wholesale business, the

Company can increase the traffic on its network more quickly, thereby generating better economic returns. Management further believes that certain segments of the wholesale market, such as ISPs, have been historically under-served by the ILECs and present very attractive growth potential.

The Company is targeting small long distance providers, PCS providers, local multi-point communication system providers, information service companies, resellers and other CLECs as wholesale customers. The Company also intends to launch competitive dedicated and switched access services to these wholesale customers for connection to end-users or for connecting carrier locations. Under the terms of the Rhythms Joint Venture Agreement, Axxent Inc. will provide DSL-based data services to small and medium-sized businesses. Rhythms Canada will market dedicated high speed DSL-based data services to large business and wholesale customers.

The wholesale segment of the market determines its supplier of services based on quality, reliability, territorial coverage, delivery and price. The Company intends to focus on the delivery of high levels of network reliability, route diversity, rapid installation and excellent customer service to its wholesale customers. The Company intends to provide services to the wholesale segment at prices below those of the ILECs, which will help to establish strong relationships with the Company's wholesale customers, and to continue to develop electronic processes to support and facilitate the ordering, provisioning and operating process.

Indirect Sales Channels

Axxent Inc. has selected a group of companies in Ontario and Quebec which operate as the Company's agents and sell Axxent Inc. products and services to their customers. These agents primarily consist of telecommunications consultants, interconnect firms and long distance resellers. Historically, approximately 35% of the Company's business had been obtained through this channel, but its contribution is now approximately 10%.

Indirect sales channels are compensated on a per line basis, as well as for long distance sales and longer contract terms.

Sales Channel Integration

The Company is currently assessing its multiple sales channels as well as its expanding data, Internet and voice product and service suites to determine the optimum distribution structure for both direct and indirect sales.

Network

The Company operates its own switch-based service provider in the principal metropolitan centres of Toronto and Montreal. Axxent Inc. will subsequently establish additional hubs in other metropolitan areas, including Vancouver, Calgary, Edmonton, Hamilton, London, Kitchener-Waterloo, Ottawa-Hull, Quebec City and Barrie.

The Company will employ the smart build strategy by deploying facilities where its customer base already exists and will continue to use its resale strategy in locations where its customer base is not large enough to profitably support a central office. Initially, Axxent Inc. will co-locate in existing ILEC central office buildings. These co-location sites will provide access to an ILEC's local loop permitting immediate coverage to all of the service area of the ILEC central office. In urban areas, such individual serving areas typically cover a radius of three to five kilometres from the co-location site.

Axxent Inc. will take advantage of DSL technology to reduce the bottleneck in the transport of information by increasing the data-carrying capacity of a single local loop by up to 100 times. Axxent Inc. will also offer high-speed data transmission to provide up to 24 lines simultaneously on each local loop leased from the ILEC. This allows the Company to provide voice and data services throughout the service area while minimizing capital expenditures.

The Company will supplement the ILEC's existing local loop with leased sonet fibre rings in those circumstances where the sonet technology provides the Company with a cost effective benefit. Sonet technology is an ultra high-speed fibre optic transmission standard for large-scale, fibre-based digital transmission networks.

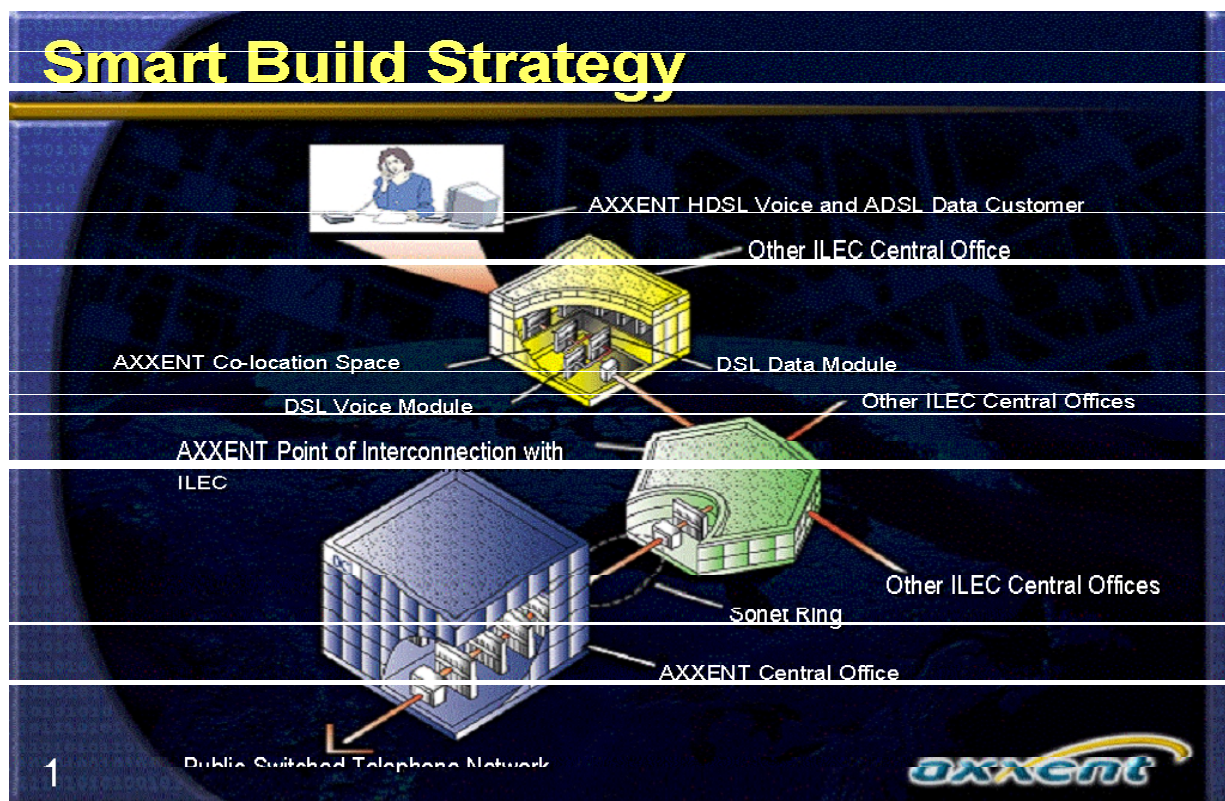
Management believes that, by deploying a switch-based network, Axxent Inc. will be able to improve margins, enhance network and service quality and broaden its range of product offerings. Ultimately, management believes that the Company's network will enable it to deliver voice and data services across a single multi-service dedicated connection. The Company also expects its network to lower customers' overall telecommunications costs and to stimulate demand for new capacity intensive services. Plans for network deployment in Ontario, Quebec, Alberta and British Columbia call for the establishment of 100 co-location sites in various ILEC central offices by the end of fiscal 2000.

The Company's first two switches, both Nortel DMS-500 switches, have been installed and are operational in Axxent Inc.'s Toronto head office and in the Company's Montreal office. Over the next two years, the Company plans to activate nine additional switches in prime market areas throughout its operating territory. The Company's network has been designed with hardware redundancy for all major network components, route diversity and automatic restoration for all backbone transmission facilities in its network.

The Toronto and Montreal switches have the ability to route local and long distance traffic with a dedicated connection to all other Axxent Inc. switches as well as the necessary ILEC switches to provide coverage for all of Ontario and Quebec. The Company is now established as a facilities-based inter-exchange carrier allowing the Company to deploy high-speed data transport equipment in these locations to supplement dial-up data services and facilitate support for a full suite of communication services in its service areas. Completion of this program will include a switch-based presence in most markets in the Company's operating territory with a population greater than 50,000 and complete coverage of the 416 area code in Toronto and the 514 area code in Montreal.

The Company is planning its local network rollout based on market opportunity and its existing resale customer base. The Company expects to extend its local network to Vancouver, Calgary, Ottawa-Hull, Hamilton, Kitchener-Waterloo and London during fiscal 2000. The Company plans to establish switches in each of those locations in addition to co-location sites in ILEC central office buildings. The Company expects that the number of ILEC co-location sites will increase to 100 by the end of fiscal 2000.

The following diagram illustrates the design of the Company's local voice and data network.



The network design illustrated above provides for local voice and data transmission. For voice transmission, a call originates with an Axxent Inc. customer and travels over the ILEC's local loop to Axxent Inc.'s co-location site in the ILEC's central office. The call then travels to the point of interconnection, being the point at which all traffic to that central office travels prior to leaving that central office. If the call is to another Axxent Inc. customer, the call remains on the Axxent Inc. network. If not, the call travels along another LEC's network to such other customer. Data transmissions are completed in the same fashion. The above diagram also illustrates the location of DSL equipment which the Company intends to use to enhance its data and voice transmission capacity.

The Company's network operation centre (the "NOC") is located within its corporate head office at 111 Peter Street, Suite 300, Toronto, Ontario. The NOC is staffed 24 hours a day, seven days a week with highly skilled technical individuals whose responsibility is to closely monitor our network elements through the operation surveillance systems, and to respond to customer problems. Axxent Inc. has deployed Micromuse Inc.'s Netcool software to monitor the Company's network on a real-time basis. Using this system, the Company is able to monitor its network for events such as alarms, alerts, lags or other faults in real-time, enabling network operators to quickly identify and address problems.

Customer Care

The Axxent Inc. customer care organization is committed to providing quality service to the Company's existing and growing customer base. Management believes that customer care excellence is a major factor in the successful operation of a CLEC. The Company has an experienced group of customer care representatives who provide customer support 24 hours a day, 365 days a year in both of Canada's official languages through the Company's customer service department in Toronto. The Axxent Inc. customer care group is trained in new order provisioning, service charges, billing, customer service and technical support in order to simplify customer contact and ensure a fast response to customer queries.

Management believes that high quality customer care will provide the Company with a competitive advantage over the ILECs and other CLECs. By offering superior customer care, management believes that the Company will retain its customers and sell additional services to its current and new customers.

The Company intends to be proactive in maintaining customer satisfaction by utilizing its sophisticated network systems which allow early detection and correction of potential network problems which could affect service to the Company's customers. The software provided by MetaSolv, In-Logic and Saville Systems will provide the backbone to the customer care system including the billing system, the provisioning and engineering system and the 411/911 system. In addition, the Company has negotiated the right to access its systems and modify presentation formats to meet its own needs.

Properties

Axxent Inc. leases its principal executive offices located at 111 Peter Street, Toronto, Ontario. The Company's Toronto switch is located at this site. The lease provides for a term of five years from March 1, 1999 to February 29, 2004 and may be renewed, at the Company's option, for two separate and consecutive terms of five years each.

Axxent Inc. is also renting office space at 1080 Cote du Beaver Hall, Suite 1510, Montreal, Quebec. The Company's Montreal switch is located at this site. The lease provides for a term of five years from January 1, 1997 to December 31, 2001.

The Company rents the following additional office space:

- 220 King Street West, Toronto, Ontario. The term of the lease is from January 1, 1998 to June 30, 2000;
- 19 Duncan Street, Toronto, Ontario. The lease provides for a term from May 1, 1997 to March 31, 2002 and may be renewed at the Company's option for an additional five-year term on at least three months' written notice;

- 277 Wellington Street, Toronto, Ontario. The term of the lease is from March 1, 2000 to February 28, 2005;
- One Yonge Street, Toronto, Ontario. The term of the lease is from February 1, 1999 to January 31, 2004;
- 30 Owen Street, Barrie, Ontario. The term of the lease is from March 29, 2000 to March 28, 2001;
- 2784 County Road 3, Ameliasburg, Ontario. The term of the lease is from March 29, 2000 to March 28, 2001;
- 211-219 Yonge Street, Toronto, Ontario. The term of the lease is from May 25, 1997 to November 30, 2000; and
- 1010 St. Catherine Street West, Dominion Square Building, Montreal, Quebec. The term of the lease is from April 1, 1997 to March 31, 2001.

The Company is also in the process of leasing a number of premises which will house its switches as part of the Company's ongoing national roll-out.

Employees

As at April 30, 2000, Axxent Inc. had 642 full-time employees. None of these employees is covered by a collective bargaining agreement or represented by a union. Management believes that the Company's relationship with its employees is good. On May 4, 2000, the Company completed the acquisition of Optimum Teleservices, adding an additional 120 telemarketers as well as a number of other representatives.

Axxent Inc. has implemented an employee share ownership plan under which all of the Company's full-time employees are granted options to purchase Class B non-voting shares upon commencement of employment. The options have been granted under the Company's share option plan. See "Management – Share Option Plan".

Acquisitions

Optimum Teleservices.

On May 4, 2000, the Company's operating subsidiary completed the acquisition of all of the issued and outstanding shares of Optimum Teleservices. Prior to the completion of such acquisition, Optimum Teleservices had been providing the Company with outbound call centre marketing services under an exclusive contract. The purchase price of the acquisition was \$5.4 million, comprised of \$2.7 million in cash and the issuance of 173,188 Class B non-voting shares, subject to adjustment in certain events.

Simcoe County Long Distance Corporation.

On March 29, 2000, the Company's operating subsidiary completed the acquisition of all of the issued and outstanding shares of Simcoe County and Quinte Long Distance Corporation. These organizations had a combined customer base of approximately 1,800 local business customers comprising more than 10,000 business lines, annual revenues of approximately \$9.0 million and a proven history of positive earnings. The purchase price of the acquisition was \$15,000,000 in cash, subject to certain adjustments. Simcoe County is the largest alternate provider of business local and telecommunication services in the Barrie, Ontario area and, through its affiliate, Quinte Long Distance, provides similar services to the Belleville, Ontario area. Management believes that the acquisition of Simcoe County will allow the Company to expand the reach of its services in Southern Ontario.

EDI Communications Networking Inc.

On March 23, 2000, Axxent Inc. completed the acquisition of all the outstanding shares of EDI Communications, an Ontario based company specializing in data network provisioning, including data network design, implementation and operations, for small and medium-sized businesses. The purchase price of the acquisition was \$4.85 million and was satisfied with the issuance of 210,938 Class B non-voting shares. At closing, Axxent Inc. held back \$400,000 of the purchase price in respect of certain post-closing adjustments and may be obligated to issue additional Class B non-voting shares at the five-day average closing price prior to such issuance. In addition, Axxent Inc. may be required to issue up to an additional \$5.65 million in Class B non-voting shares if certain performance targets are met. The number of shares to be issued will be determined using the five-day average closing price for the Class B non-voting shares immediately prior to the date of issue. Pursuant to a purchase agreement dated June 8, 2000, Axxent Inc. transferred all of the issued and outstanding shares of EDI Communications to Axxent Corp. in exchange for 211,237 common shares of Axxent Corp.

Pathway Communications.

On July 29, 1999, the Company's operating subsidiary acquired all of the issued and outstanding shares of Pathway, a Toronto-based ISP that also provides network integration and other Internet-related services. Management believes that the integration of Pathway's business will provide Axxent Inc. with an opportunity to capitalize on its target market of small and medium-sized businesses while enabling it to provide services to the ISP market.

Axxent Inc. acquired Pathway for consideration at closing consisting of a payment of \$3.5 million cash and the issuance of Series 1 preferred shares and Series 2 preferred shares which were convertible into an aggregate of 416,667 Class B non-voting shares. The Company qualified the distribution in Ontario of the 416,667 Class B non-voting shares issued upon conversion of the Series 1 and Series 2 preferred shares in December 1999. In addition, on February 11, 2000, the Company paid to the former Pathway shareholders an additional \$200,000 and issued them 33,333 Pathway Special Warrants exercisable, for no additional consideration, for 33,333 Class B non-voting shares which were valued at \$200,000 at the time of closing of the acquisition. This prospectus qualifies the issuance of the Class B non-voting shares to be issued upon exercise of the Pathway Special Warrants. The Company has also agreed to pay, on January 24, 2001, to the Pathway shareholders a final payment of \$200,000 and to issue special warrants exercisable, for no additional consideration, for 33,333 Class B non-voting shares which were valued at \$200,000 at the time of closing of the acquisition.

Canadian Telecom Resellers Alliance.

On June 17, 1999, the Company's operating subsidiary acquired all of the issued and outstanding shares of CTRA through the acquisition of all of the outstanding shares of Oakbrook Communications Inc. CTRA is a start-up wholesale long distance reseller that has negotiated aggressive pricing from long distance carriers which it resells at a mark-up to small long distance resellers.

The CTRA purchase agreement provided for aggregate cash consideration at closing of \$500,000 and the issuance at closing of warrants (the "CTRA Warrants") to purchase 416,667 Class B non-voting shares at an exercise price of \$6.00 per Class B non-voting share. Axxent Inc. will issue additional CTRA Warrants to purchase up to 250,000 Class B non-voting shares with an exercise price of \$6.00 if certain specified monthly revenue thresholds are achieved prior to November 30, 2000.

Competition

Axxent Inc. faces intense competition for its existing and planned services from:

- the ILECs;
- other CLECs;

- cable companies;
- competitive long distance providers;
- wireless service providers;
- Centrex resellers; and
- ISPs, including those ISPs seeking access to the high-speed Internet services offered by LECs and cable companies.

Management believes that the CRTC Local Competition Decision has accelerated competition for all types of local switched services which are currently dominated by the ILECs. In addition, the majority of Axxent Inc.'s competitors, both current and potential, have both longer operating histories in the Canadian telecommunications industry and greater resources than the Company's. See "Industry Background" and "Risk Factors".

ILECs

The ILECs, which are vertically-integrated telephone companies, represent Axxent Inc.'s most significant competition for business customers throughout Canada. The ILECs include such companies as Bell Canada and TELUS Communications Inc. The ILECs have greater resources than the Company and have long-standing relationships with their customers. Although ILECs are generally subject to greater pricing and regulatory constraints than CLECs, ILECs have, as a result of the price cap decision released by the CRTC at the same time as the Local Competition Decision (the "Price Cap Decision"), achieved increased pricing flexibility for their services. The Price Cap Decision brought most of the ILECs' local services under a price cap regime intended to improve ILEC productivity by limiting annual price changes on capped services. In particular, since ILECs need not include the mandated 25% mark-up that they charge to CLECs for non-essential services in their own floor prices, ILECs are able to compete against the CLECs which rely on such non-essential services on the basis of price alone if they see fit to do so. If the ILECs lower rates or engage in substantial volume and term discount pricing practices, there will be downward pressure on certain of Axxent Inc.'s rates, which could have a material adverse effect on the Company's business, financial condition and results of operation.

Until the Local Competition Decision allowed competition in Canadian local markets, the ILECs did not compete with each other. Each ILEC, with the exception of Bell Canada, which operates in both Ontario and Quebec, effectively operated in a single province. Management believes that BCE Inc.'s (Bell Canada's parent company) decision in April 1998 to offer high-speed data and Internet services directly to business customers over a national broadband network following the break-up of the ILEC's Stentor alliance will likely mean that the ILECs will compete among themselves as well as with new entrants. Furthermore, BC Tel (serving British Columbia) and TELUS (serving Alberta) have merged and have begun pursuing a national presence. In addition, the ILECs in the Atlantic provinces of Canada have merged to form one organization that will have the resources to compete in the redefined marketplace.

Management also believes that the ILECs' ability to compete in both the wireline and wireless markets was improved with the removal in March 1998 of the prohibition against their joint marketing of wireless and wireline services. The CRTC has also granted the ILECs more flexibility in bundling monopoly local and competitive services under certain restrictions.

CLECs

As at June 2, 2000, there are 15 companies who have met the CRTC requirements to operate as CLECs in Canada. The 15 are Axxent Inc., AT&T Canada Inc. ("AT&T Canada"), C1.com Inc., Gateway Telephone Limited, Call-Net Communications Inc., GT Group Telecom Services Corp., Vidéotron Telecom (1998) Ltée., East Link Limited, Futureway Communications Inc., Bell Intrigna Inc., Maskatel Inc., Norigen Communications Inc., Novus Telecom Inc. and Vidéotron (1998) Ltée. In addition, management believes that, as of June 2, 2000, there were 27 companies that had announced their intention to become CLECs in Canada.

Cable Companies

Incumbent cable companies, including Videotron Telecom, Shaw Cablesystems Ltd. Inc., Rogers Cablesystems and Cogeco Cable Systems Inc., may compete with Axxent Inc. in certain of its markets. Many cable companies have greater resources than Axxent Inc. and have established customer contracts. No single cable company currently operates nationally, although several of the major cable companies have formed an alliance to establish national standards for new products and services and to provide a unified marketing force to more effectively compete against the ILECs. Many of the major cable companies have competitive access divisions or an affiliate providing dedicated access, private lines and data transmission services. Certain cable companies have purchased digital switches and have deployed fibre optic networks in their cable service area.

Competitive Long Distance Providers

Aside from the ILECs, the major long distance providers include AT&T Canada and Call-Net and, in the residential market, Primus Telecommunications. These companies have sales offices and/or agents located in each of the Company's target markets and have achieved significant market share gains in the long distance market. In December, 1999, AT&T Canada announced that it had launched an ADSL Internet access service for businesses, the first in its planned roll-out of DSL-based services to approximately 80% of the business access lines across Canada by the end of 2000.

Management believes that competition in the long distance market will continue to intensify following the development of local competition, mergers in the industry and the decision of CRTC to relax its regulation of most long distance services provided by the ILECs and their competitors.

Wireless Service Providers

As equipment costs and service rates continue to decline in the wireless services industry, the Company expects to face increasing competition in the local telecommunications market from wireless service providers. Management believes that wireless service providers will increasingly offer products that compete directly with traditional wireline services. For example, Microcell Telecommunications Inc. ("Microcell") has announced its intention to operate as a wireless CLEC.

There are currently four nation-wide wireless mobile service providers operating in Canada. Rogers Mobile Communications Cantel Inc. and the ILEC-controlled mobile service operators comprising Mobility Canada are the incumbent cellular providers and have been awarded PCS licenses. Two more recent entrants, Microcell and Clearnet Communications Inc., have deployed personal communications services aggressively in metropolitan markets throughout Canada. Industry Canada recently completed a wireless auction for the 24 and 38 GHz spectrums. Access to these spectrums will permit licensees to offer broadband wireless services including high-speed Internet video teleconferencing, wireless local loop and e-commerce applications. Of the 13 companies participating in the auction, 12 were awarded a total of 260 licenses to utilize this spectrum to offer broadband wireless services across Canada. However, the success of these companies in this spectrum is still very early stage and uncertain. In addition, Industry Canada has announced that it intends to hold another spectrum license auction in the fall of 2000 for additional PCS spectrum in the 2 GHz frequency range. The purpose of making this additional spectrum available is to facilitate the expansion and enhancement of existing PCS services and the introduction of third generation PCS and other services to allow a wide range of multimedia wireless services including Internet applications and video-oriented services.

Internet Service Providers

Competition for business Internet and e-commerce services is strong. The subsidiaries of U.S. Internet companies such as AOL Canada Inc. ("AOL Canada"), Netcom Global Marketing Inc., PSINet Limited and UUNet Canada Inc. have traditionally focused on the large business market. The over 500 privately-owned small, local Canadian ISPs, the largest of which have been acquired by the U.S. Internet companies and emerging Canadian CLECs, have targeted the small and medium-sized business markets by offering a range of low-cost offerings. Telephone

companies, such as AT&T Canada, Call-Net (Sprint Canada) and Bell Canada with its Sympatico service, AOL Canada and the cable companies continue to focus primarily on the residential markets. Providers who have carved a successful niche for themselves have expanded their services beyond mere delivery of bandwidth to offer bundled, value-added services. Management believes that, currently, none of these ISPs combine Internet, e-commerce and network services to the desktop or manage Internet servers inside the customer's premises and that there is a substantial market for these services in the small to medium-sized business segment.

New Entrants and Alliances

Axxent Inc. could also face competition from new entrants, including:

- new Canadian CLECs, including alliances of existing competitors;
- U.S. LECs which may, subject to regulatory requirements restricting foreign ownership, enter the major cities in the Canadian market; and
- power and energy utilities which often own valuable rights-of-way and which management believes are seeking alternative sources of revenue.

The Company is not aware of any major Canadian electric utilities planning to compete in the switched local market. Both Hydro One Inc. (the successor to the transmission and distribution business of Ontario Hydro) and Hydro Quebec have fibre optic facilities for telecommunications purposes and have indicated they are interested in marketing telecommunications services.

Canadian telecommunications foreign ownership requirements limit the ability of non-Canadian long distance providers to enter the Canadian market. However, such ownership requirements have not prevented major U.S. long distance providers such as Ameritech Corporation, AT&T Corp. and Sprint from entering the Canadian market through non-controlling equity investments in Canadian companies. Further, resellers, which are not subject to regulation by the CRTC, are permitted to be 100% owned by non-Canadians. Currently, a large portion of the long distance services market that is not controlled by ILECs is controlled by companies which have formed alliances with U.S. long distance providers.

Legal Proceedings

The Company is not currently a party to any material litigation or administrative proceedings other than regulatory proceedings in the normal course of business.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

You should read the following discussion and analysis together with the consolidated financial statements of the Company, including the notes and the other financial information appearing elsewhere in this prospectus.

Overview

Axxent Inc. is a Canadian telecommunications provider of voice, data and Internet services. The Company targets small and medium-sized businesses, a sector that management believes is under-served by the ILECs and which management believes has significant revenue and profit potential. In pursuit of the Company's growth strategy, Axxent Inc.'s operating subsidiary has met all of the requirements of the CRTC to operate as a CLEC in Canada. To facilitate the Company's early market entry, Axxent Inc. began offering local voice services by reselling the services of the ILECs in January 1995.

Axxent Inc. operates its own switching equipment in the Company's head office in Toronto as well as in the Company's Montreal office. As the Company expands, it will continue to use the resale of voice services as its strategy for building enough customer density to ensure that the use of the Company's own facilities will be economically attractive.

Revenues

Through March 31, 2000, the Company generated the majority all of its revenue from the resale of local and long distance voice services, primarily to small and medium-sized businesses. The Company has recently begun to offer Internet and data services in certain portions of its market. In addition, the Company has recently commenced the deployment of its own network. Despite declining prices for local and long distance services due to increasing competition, the Company expects margins on local service to increase as the Company commences the migration of its existing customers from resale to the Company's local facilities.

In future periods, the Company expects the resale of local services to constitute a decreasing portion of its total revenue, as local services revenue from its own switching facilities and revenue from its data and Internet services begin to develop. In addition, the Company expects revenue from wholesale services to increase, both in the voice and data markets.

Operating Expenses

The Company's operating costs consist of cost of services, selling, general and administrative ("SG&A") costs and amortization and depreciation costs.

Cost of Services. Through March 31, 2000, cost of services consisted of expenditures to the underlying carriers of the local and long distance services that Axxent Inc. resells to customers. The three main carriers selling services to the Company are Bell Canada, Call-Net and AT&T Canada. For future periods, cost of services will also include the fixed costs of leased facilities and the variable costs of origination, termination and access services provided through LECs and other telecommunications companies. Cost of services will also include the fixed costs of other network elements.

SG&A Costs. SG&A costs include the personnel costs to acquire and retain customers, billing costs, premises costs and related administrative expenses.

Depreciation and Amortization. Depreciation and amortization expense includes depreciation and amortization of new customer conversion fees paid to Bell Canada, plus amortization of capital assets including computer hardware and software, office equipment and leasehold improvements and, for periods after June 30, 1999, switching equipment and facilities. Conversion fees have been amortized over 24 months which has been the average

term of the Company's customer contracts. Goodwill of \$26.0 million resulting from the various acquisitions will be amortized over seven years.

Throughout the Company's history, Axxent Inc. has experienced operating losses and generated negative cash flow. All expenditures directly related to the acquisition of new customers other than the conversion fees are expensed when incurred.

Rhythms Canada Joint Venture

In January 2000, the Company entered into the Rhythms Canada joint venture. As a 50% common equity owner, the Company will recognize a proportionate share of Rhythms Canada's revenue, expenses and income or loss. In addition, the Company is entitled to receive dividends, at a cumulative rate of 6%, on the U.S.\$10.0 million of preferred shares the Company purchased in Rhythms Canada, which will constitute other income if and when paid. See "Business of the Company – Rhythms Canada Joint Venture".

Results of Operations

Six Month Period Ended March 31, 2000, compared with Six Month Period Ended March 31, 1999

Revenue: Revenue for the six months ended March 31, 2000 was \$29.9 million, a 40% increase over revenue of \$21.3 million for the six months ended March 31, 1999. This increase was due to growth in the number of business customers that the Company serves, which grew by 93% to 25,546 from 13,261 for the six months ended March 31, 1999. Increases in revenue were a result of continued strong sales results and low customer attrition, and the acquisition of various companies.

Local line revenue for the six months ended March 31, 2000 represented approximately 69% of total revenue or \$20.6 million compared to \$16.7 million or 78% for the six months ended March 31, 1999. Revenue from outbound long distance and toll-free services for the six months ended March 31, 2000 was \$6.3 million compared to \$4.7 million for the six months ended March 31, 1999. Internet and related data services revenue totalled \$3.0 million for the six months ended March 31, 2000 compared to no such revenue in the prior year.

Cost of Services: Cost of services for the six months ended March 31, 2000 increased to \$22.5 million, from \$15.6 million for the six months ended March 31, 1999 due primarily to growth in the number of customers that the Company serves. Overall gross margins for the six months ended March 31, 2000 were 25% compared to 27% for the six months ended March 31, 1999.

Local line margins for the six months ended March 31, 2000 were 16% compared to 24% for the six months ended March 31, 1999. This decrease in local line margins is primarily attributable to the transition to on-net service and reflects initial over-capacity in the network. Long distance margins declined to 30% from 38% in 1999 with the addition of our lower margin wholesale business. Gross margins on Internet and related data services for the six months ended March 31, 2000 were 74%.

Selling, General and Administrative Costs: Total SG&A expenses for the six months ended March 31, 2000 were \$28.3 million compared with \$9.4 million for the six months ended March 31, 1999 due to the Company's expanded sales efforts and growth in the number of customers that the Company serves. Increased SG&A costs were primarily a result of higher salaries and wages and related expenses due to increased staff levels to acquire and maintain a larger customer base and due to costs associated with the launch of the Company's facilities-based services.

Depreciation and Amortization: Depreciation and amortization expense for the six months ended March 31, 2000 was \$5.6 million compared to \$1.2 million for the six months ended March 31, 1999.

Interest Income: Interest income for the six months ended March 31, 2000 increased to \$2.0 million from \$0.6 million for the six months ended March 31, 1999, reflecting the interest income on investments held from the proceeds of the Company's initial public offering and the Special Warrant offering completed in March 2000.

Interest Expense: Interest expense for the six months ended March 31, 2000 increased to \$4.7 million from \$3.9 million for the six months ended March 31, 1999 reflecting interest accrued on the 1997 notes.

Foreign Exchange (Gain) Loss: Foreign exchange gain was \$0.1 million for the six months ended March 31, 2000 compared to a loss of \$0.1 million for the six months ended March 31, 1999.

Fiscal Year ended September 30, 1999, compared with Fiscal Year Ended September 30, 1998

Revenue: Revenue for fiscal year 1999 was \$45.9 million, a 45% increase over revenue of \$31.7 million in fiscal year 1998. This increase was due to growth in the number of business customers that the Company serves, which grew by 52% to 17,646 (including Internet customers) from 11,622 in fiscal year 1998. The number of lines in service on September 30, 1999 was 71,939 compared to 52,848 on September 30, 1998. Increases in revenue were due to continued strong sales results and low customer attrition in the Toronto market and to new secondary markets being added in Ontario and Quebec.

Local line revenue for fiscal year 1999 represented approximately 77% of total revenue or \$35.3 million, compared to \$23.6 million or 74% in fiscal year 1998. Revenue from outbound long distance and toll-free services in fiscal year 1999 was \$9.9 million compared to \$8.1 million in fiscal year 1998.

Cost of Services: Cost of services in fiscal year 1999 increased to \$33.9 million from \$23.6 million in fiscal year 1998 due to growth in the number of customers that the Company serves. Overall gross margins were 26% for fiscal year 1999 and fiscal year 1998.

Local line margins were 21% in fiscal year, 1999 compared to 28% in fiscal year 1998 while long distance margins improved to 40% from 35 % in fiscal year 1998.

Selling, General and Administrative Costs: Total SG&A expenses in fiscal year 1999 were \$27.2 million compared with \$14.1 million in fiscal year 1998. The increase was due to the Company's expanded sales efforts and growth in the number of customers that the Company serves. Increased SG&A costs were primarily a result of higher salaries and wages and related expenses due to increased staff levels to acquire and maintain a larger customer base and due to the costs associated with the launch of the Company's facilities-based services.

Depreciation and Amortization: Depreciation and amortization expense in fiscal year 1999 increased to \$4.0 million compared to \$1.9 million in fiscal year 1998 due to capital expenditures driven by expansion.

Interest Income: Interest income in fiscal year 1999 increased to \$1.5 million from \$1.3 million in fiscal year 1998, reflecting the interest income on investments held from the issuance of the 1997 notes and the April 1999 special warrant offering.

Interest Expense: Interest expense in fiscal year 1999 increased to \$8.4 million from \$6.5 million in fiscal year 1998 reflecting interest associated with the 1997 notes.

Financing Expenses: Financing expenses in fiscal year 1999 were \$0.8 million compared to \$3.7 in fiscal year 1998. This expense was associated with a consent solicitation statement and payment in connection with the 1997 notes.

Foreign Exchange (Gain) Loss: Foreign exchange loss was \$0.3 million for fiscal year 1999 compared to a loss of \$0.1 million in fiscal year 1998.

Fiscal Year Ended September 30, 1998, compared with Fiscal Year Ended September 30, 1997

Revenue: Revenue for fiscal year 1998 was \$31.7 million, a 144% increase over revenues of \$13.0 million in fiscal year 1997. This increase was due to growth in the number of customers that the Company serves, which grew by

45% to 11,622 from 8,022 in fiscal year 1997. The number of lines in service on September 30, 1998 was 52,848 compared to 25,838 on September 30, 1997. Increases in revenue were a result of continued strong sales results and low customer attrition in the Toronto market in addition to new secondary markets being added in Ontario and Quebec.

Local revenue represented approximately 74% of total revenue or \$23.6 million for fiscal year 1998, versus \$10.2 million or 78% in fiscal year 1997. Revenue from outbound long distance and toll-free services were \$8.1 million in fiscal year 1998 compared to \$2.8 million in fiscal year 1997.

Cost of Services: Cost of services increased to \$23.6 million in fiscal year 1998, from \$10.0 million in fiscal year 1997 due to growth in the number of customers that the Company serves. Overall gross margins in fiscal year 1998 were 26% compared to 23% in fiscal year 1997. The improvement in gross margins was a result of volume increases and resulting discounts in long distance cost.

Local loop margins were 28% in fiscal year, 1998 compared to 31% in fiscal year 1997 while long distance margins improved to 35% from 20% in fiscal year 1997. Overall margins were 26% due to the approximate 5% gross margin on resale services from Bell Canada.

Selling, General and Administrative: Total SG&A expenses in fiscal year 1998 were \$14.2 million compared with \$6.7 million in fiscal year 1997. The increase was due to the Company's expanded sales efforts and growth in the number of customers that the Company serves. Increased SG&A costs were primarily a result of higher salary and wages and related expenses due to increased staff levels to acquire and maintain a larger customer base.

Depreciation and Amortization: Depreciation and amortization expense increased to \$1.9 million in fiscal year 1998 from \$0.7 million in fiscal year 1997 due to increased customer conversion costs and increased capital expenditures driven by expansion.

Interest Income: Interest income increased to \$1.3 million in fiscal year 1998 from nil in fiscal year 1997, reflecting the interest income on investments held from the issuance of the 1997 Notes.

Interest Expense: Interest expense increased to \$6.5 million in fiscal year 1998 from \$0.6 million in fiscal year 1997 reflecting interest associated with the 1997 Notes issued on December 31, 1997, a bridge loan and shareholders' loans (described under "Liquidity and Capital Resources").

Financing Expenses: Financing expenses were \$3.7 million in fiscal year 1998 compared to nil in fiscal year 1997. This expense was associated with the issuance of the 1997 Notes.

Foreign Exchange (Gain) Loss: Foreign Exchange Loss was \$0.1 million for fiscal year 1998 compared to nil for fiscal year 1997.

Quarterly Results of Operations

The following table summarizes selected quarterly financial information for the Company's eight most recent fiscal quarters. This information is unaudited, but reflects all adjustments of a normal, recurring nature which are, in the opinion of management, necessary to present a fair statement of the Company's results of operations for the periods presented. Quarter-to-quarter comparisons of the Company's financial results are not necessarily meaningful and should not be relied upon as an indication of future performance.

	June 30, 1998	September 30, 1998	December 31, 1998	March 31, 1999	June 30, 1999	September 30, 1999	December 31, 1999	March 31, 2000
	(dollars in thousands)							
	(unaudited)							
Statement of Operations Data:								
Revenue.....	\$ 8,729	\$ 9,212	\$10,512	\$10,796	\$11,375	\$13,177	\$14,077	\$15,775
Expenses:								
Cost of services.....	6,479	6,809	7,593	7,998	8,712	9,599	10,744	11,760
Selling, general and administrative	4,237	3,998	4,323	5,032	6,464	11,290	12,520	15,802
Depreciation and amortization ..	509	661	568	595	913	1,891	2,455	3,135
Loss before undernoted.....	(2,496)	(2,256)	(1,972)	(2,829)	(4,714)	(9,603)	(11,642)	(14,922)
Other Income (expense):								
Interest income.....	516	374	346	283	498	395	945	1,063
Interest expense.....	(1,903)	(1,922)	(1,939)	(1,990)	(2,220)	(2,502)	(2,159)	(2,511)
Foreign exchange gain (loss)	0	0	0	(155)	0	(147)	(170)	297
Financing expenses.....	0	(81)	16	0	(855)	0	0	0
Net loss.....	(3,883)	(3,885)	(3,549)	(4,691)	(7,291)	(11,857)	(13,026)	(16,073)

Liquidity and Capital Resources

The Company's current assets of \$231.5 million at March 31, 2000, including cash and short term investments of \$208.9 million, exceeded current liabilities of \$25.8 million at March 31, 2000. This provided a working capital surplus of \$205.7 million at March 31, 2000 compared to a working capital surplus of \$10.2 million at September 30, 1999. The increase in working capital was attributable to the completion of the November 1999 initial public offering for gross proceeds of \$115.2 million and the completion of the special warrants on March 28, 2000 for gross process of \$180.0 million, partially offset by the continued development of the Company's network, operating losses, working capital requirements and interest payments.

Previous Financings

The Company's voice reselling operations did not generate sufficient cash flow from its inception in 1994 through March 31, 2000 to enable Axxent Inc. to meet all of its capital expenditure, debt service and other cash needs. During this period, cash for these requirements was provided primarily by the equity and debt financings described below.

To date, the Company has raised net proceeds of approximately \$395.0 million in debt and equity capital financings to fund the Company's business plan, deployment of the network and cash losses from operations including net proceeds of approximately \$322.0 million from equity capital financings and net proceeds of approximately \$52.0 million from the issuance of the 1997 Notes and related Note Warrants.

Private Equity Investment. In a September 1996 private placement, the Company's operating subsidiary issued 5,000,000 common shares for gross proceeds of \$2.5 million to five purchasers and granted options for an additional 5,000,000 common shares. The options were exercised in early 1997 for an additional \$2.5 million in cash. These common shares were exchanged, on a one-for-one basis, for Class A voting shares of the Company in connection with the reorganization of Axxent Inc. completed on April 1, 1999.

1997 Private Placement. In a December 1997 private placement, the Company's operating subsidiary issued 30,000 units, each consisting of US \$1,000 principal amount of a U.S. dollar denominated senior note and 213.3 Note Warrants and 7.162 units each consisting of \$1,000 principal amount of a Cdn. dollar denominated senior note and 213.3 Note Warrants to acquire common shares of the Company's operating subsidiary for an aggregate purchase price of U.S. \$30.0 million plus approximately \$7.2 million. Each three Note Warrants entitle the holder thereof to acquire one common share of the Company's operating subsidiary at a purchase price of \$0.03 per common share. The Company has agreed with the holders of the 1997 Notes to acquire from any holder requesting to do so all but not less

than all of the Note Warrants held by such holders in exchange for Series 3 preferred shares. Each Series 3 preferred share will be convertible into one Class B non-voting share upon payment of \$0.03 per share.

1999 Special Warrants. In April 1999, the Company issued 17,410,000 special warrants for gross proceeds of approximately \$34.8 million. In December 1999, the special warrants were automatically exercised, for no additional consideration, for an aggregate of 5,803,333 Class A voting shares. The Company qualified the distribution of the Class A voting shares issuable upon exercise of the special warrants under a prospectus dated December 9, 1999.

Rhythms Special Warrants. On October 27, 1999, Axxent Inc. issued the Rhythms Special Warrant for gross proceeds of US\$5.3 million. In December 1999, the Rhythms Special Warrant was automatically exercised, for no additional consideration, for 763,680 Class B non-voting shares. The Company qualified the distribution of the Class B non-voting shares issuable upon exercise of the Rhythms Special Warrant under a prospectus dated December 9, 1999.

Initial Public Offering. On October 28, 1999, the Company filed a (final) prospectus in all provinces of Canada qualifying the issuance and sale, by way of initial public offering, of 8,400,000 Class B non-voting shares for gross proceeds of \$100.8 million. This offering closed on November 4, 1999. On December 22, 1999, the underwriters of the initial public offering exercised an over-allotment option granted to them in connection with the initial public offering for 1,260,000 Class B non-voting shares for additional gross proceeds of \$15.1 million.

Special Warrants. In March 2000, the Company issued the Special Warrants for gross proceeds of \$180 million. The Special Warrants are exercisable, for no additional consideration, for an aggregate of 10,000,000 Class B non-voting shares, subject to adjustment in certain events.

Capital Requirements

The CLEC business is capital intensive. The Company's operations will continue to require substantial capital to fund the development and deployment of its network and services in Canada, to fund the continued execution of its business plan and for other general corporate purposes, including funding operating losses, acquisitions and working capital needs. Axxent Inc. plans to continue deploying capital for the development of its network in order to offer voice, data and Internet services in those markets. The Company's capital expenditures are expected to be approximately \$140 million during the current fiscal year which ends on September 30, 2000. The majority of these expenditures will be made to continue to build out the Company's network and develop appropriate information systems.

Management believes that the Company's cash, together with the net proceeds of its initial public offering and the Special Warrant offering, will provide Axxent Inc. with sufficient liquidity to fund capital expenditures, operating losses and working capital requirements beyond the end of the year 2000. The Company can give no assurance in this regard and such estimate is subject to change upon completion of the business plan for the proposed joint venture with Rhythms. Thereafter, the Company may require additional financing. The extent of additional financing required will depend upon the rate of Axxent Inc.'s expansion and the success of Axxent Inc.'s business.

However, in the event that the Company's plans change, the assumptions upon which the Company's plans are based prove inaccurate, the Company expands or accelerates its business plan or determines to consummate new acquisitions, the foregoing sources of funds may prove insufficient to complete the networks planned to be completed over the next 12 months, and the Company may be required to seek additional financing sooner than is currently expected. Additional sources of financing may include public or private equity or debt financing, capitalized leases and other financing arrangements. In addition, the Company is currently in discussions with Nortel in order to explore possible financing alternatives.

Axxent Inc. can give no assurances that additional financing will be available to the Company or, if available, that such additional financing can be obtained on a timely basis on acceptable terms or within the limitations contained in the 1997 Notes, or any future financing arrangements. Failure to obtain such financing could result in the delay or abandonment of some or all of the Company's development and expansion plans and expenditures, which would have a material adverse effect on the Company's business, financial condition and results of operations. Such failure could also

limit the Company's ability to make principal and interest payments on the Company's indebtedness. See "Risk Factors".

Foreign Currency Translation and Hedging

Axxent Inc. is exposed to foreign currency risks. Substantially all revenues and corresponding receivables are in Canadian dollars. However, the 1997 Notes are primarily denominated in U.S. dollars. Such U.S. denominated long term debt is hedged with a foreign currency option contract which can be exercised at any time until January 2, 2001. As of March 31, 2000, there was \$0.55 million unrealised gain on the option contract.

While the Company expects to continue to use its current method of hedging foreign currency risk in the future, it may change the hedging methodology. If the Company's currency requirements differ materially from current hedged positions during periods of currency volatility or if the Company does not continue to hedge Canadian currency commitments or if it fails to retire the 1997 Notes prior to the January 2, 2001 maturity of the option contract, the Company could experience unanticipated currency gains or losses.

Axxent Inc. assumes the risk relating to the creditworthiness of the Company's counterparties when Axxent Inc. engages in hedging transactions. Axxent Inc. mitigates this risk by dealing only with substantial commercial banks it believe to be creditworthy. The Company does not believe that the credit risk associated with these transactions is material.

Year 2000 Compliance

The Year 2000 problem arose from the fact that many computer programs indicated the year by only two digits, rather than four. As a result, it was generally thought that computer systems and software in a wide variety of industries would possibly produce some erroneous results unless they were modified or upgraded to process data information correctly. Prior to December 31, 1999, the Company conducted a Year 2000 compliance investigation covering all network equipment used to provide services to its customers, network operations and support systems used to support the operations of its network, and all administrative support systems. As of the date of this prospectus, the Company has not encountered any Year 2000 related problems. The Company continues to monitor developments in this area. Management believes that the Company's most significant Year 2000 risk lies with the Company's customers and major suppliers. The Company has developed a contingency plan to minimize operational problems if Year 2000 related problems arise.

Costs. Costs incurred to date have primarily consisted of labour from redeployment of existing information services and operational resources which been expensed as incurred. The costs of new billing software, operational software and financial and personnel software systems, which are key to the Company's year 2000 compliance and which Axxent Inc. is implementing as a result of the expansion of its business, will be capitalized in accordance with GAAP. The Company does not expect that future costs will have a material adverse affect on the financial data as presented.

REGULATION

CRTC and Legislation

Companies which own or operate transmission facilities in Canada over which communication services are provided to the public are classified as Canadian carriers (“carriers”) under the *Telecommunications Act* (Canada) (the “*Telecommunications Act*”). The CRTC is Canada’s federal telecommunications regulator and has the mandate to approve or deny the terms, conditions, rates and charges applicable to services provided by carriers, as well as to dictate the terms of competition in the telecommunications market. Resellers, which do not own or operate, but merely lease transmission facilities or services from carriers for resale, are not regulated directly by the CRTC.

The CRTC has jurisdiction over all telecommunications services provided by carriers. The sole exception to this general rule was in Saskatchewan, where the incumbent carrier, SaskTel, is owned by the provincial government. However, effective June 30, 2000, SaskTel will come under the federal jurisdiction of the CRTC.

The *Telecommunications Act* provides the CRTC with the power to forbear or refrain from exercising certain of its regulatory powers, including regulating rates, when it finds that competition is or will be sufficient to protect the interests of end-customers. Certain carriers, such as the ILECs, are considered dominant by the CRTC because of their market power and control over the supply of local services and certain long distance services. Carriers classified as non-dominant by the CRTC are generally subject to less regulation than dominant carriers. Non-dominant carriers include:

- alternate providers of long distance services, such as AT&T Canada and Call-Net (Sprint Canada);
- CLECs such as Axxent Corp., GT Group Telecom Services Corp., Norigen Communications Inc., Call-Net and AT&T Canada; and
- competitive access providers such as Shaw FiberLink.

The CRTC has refrained from regulating the rates charged by non-dominant carriers for all services, other than the rates charged by CLECs to other carriers. The CRTC refrained from regulating certain services provided by ILECs, including certain packet data services, discount long distance services, retail Internet services and many long distance private line services. In addition to its power to forbear from regulating, the CRTC also has the power to exempt any class of carrier from the application of the *Telecommunications Act* if such an exemption is consistent with Canadian telecommunications policy objectives. To date, the CRTC has not exercised this power.

Leave to appeal decisions of the CRTC may be sought from the Federal Court of Appeal. CRTC decisions may equally be challenged by petition to the Cabinet of the Government of Canada. The CRTC has the power to review and vary its own decisions, either on its own initiative or by way of an application initiated by a party. Applications to review and vary CRTC decisions must generally be brought within six months of a decision being rendered. However, applications to alter a ruling made by the CRTC can be brought at any time on sufficient grounds.

Framework for Competition in Local Services

Facilities-based competition has existed in the long distance market in Canada since 1992. In 1994, the CRTC determined that competition should be permitted in the local switched telephone market as well. In May 1997, the CRTC issued two significant decisions, one of which, the Local Competition Decision, established the framework for competition in the provision of local switched telephone services. The other decision, the Price Cap Decision, established a new regime for regulating the ILECs’ existing monopoly local services. These decisions did not apply to SaskTel or to the relatively smaller ILECs serving generally rural or remote communities referred to as the Independents.

The Local Competition Decision established a comprehensive regulatory framework that addresses most of the key issues necessary to permit competition in the local phone market. This decision has since been subject to further refinement in terms of its implementation and it is expected that it will continue to evolve as competition takes root. The

following is a summary of the major features of the Local Competition Decision which are expected to have a material impact on the Company's business.

Co-carrier Status

In the local telephone market, the CRTC considers CLECs to be carriers of equal stature with, and not merely customers of, the ILECs. Accordingly, the CRTC mandated that ILECs and CLECs terminate each others' traffic originating within the same ILEC exchange based on bill and keep arrangements. These arrangements do not require the LECs originating traffic to compensate other LECs for terminating their traffic within the same local exchange unless there is a substantial traffic imbalance for a significant period of time. In areas in which terminating traffic is at a substantial imbalance, LECs charge each other for the imbalance in traffic termination functions that they perform using cost-justified rate levels approved by the CRTC.

The CRTC determined that ILECs and CLECs must each identify the point of interconnection within the ILEC local exchange for all local exchanges in which CLECs plan to provide service. The point of interconnection is the location where LECs' respective networks interconnect for the exchange of traffic. The Company has designated its point of interconnection with Bell Canada's local network as 111 Peter Street, Toronto. The CRTC also directed that LECs should share the cost of this interconnection equally. To this effect, the Company has entered into an interconnection agreement with Bell Canada.

Unbundling of ILEC Facilities

In order to provide service, CLECs require access to or the use of certain discrete elements of the ILECs' local exchange network, referred to as unbundled facilities. The CRTC, in the Local Competition Decision, ordered the ILECs to make available to CLECs the following unbundled facilities, which they deemed as essential in providing local switched services:

- central office codes;
- subscriber directory listings; and
- local loops in several high-cost small urban and rural areas.

The CRTC determined that other facilities of the ILECs' networks, though not essential, were nevertheless necessary during the early years of competition, and directed the ILECs to make them available to CLECs as if they were essential. These facilities include all urban local loops, other than those deemed essential, and traffic transiting services. Services such as the inside wire to the end-users, local switching, directory assistance and 9-1-1 service were deemed by the CRTC as non-essential. However, the CRTC required the ILECs to make inside wire available to the customer's chosen service provider.

The CRTC directed the ILECs to price both essential services and these specified non-essential facilities at long-run incremental costs, plus a 25% mark-up, which are known as essential facilities rates.

The Local Competition Decision requires that the specified non-essential facilities be unbundled and offered at essential facilities rates for five years from the time of the decision. The Company expects that, prior to the end of this five-year period, the issue of whether to extend this five-year period will be raised before the CRTC. Any proceeding to consider this issue will likely be very contentious and controversial.

The mandatory unbundling of ILEC facilities enables Axxent Inc. to lease these facilities in order to provide service to customers not reached by its network. Management estimates that approximately two-thirds of the switched lines the Company uses to provide local service to Axxent Inc. customers will be unbundled local loops leased from the ILECs. Accordingly, and because the local loops located in Axxent Inc.'s initial markets are not considered essential by the CRTC, before the expiration of the five-year period the Company will have to either reach agreements with the relevant ILECs to continue leasing these local loops, which may be on less favourable terms than the CRTC-mandated

rates for essential services, or develop other alternatives to reach these customers, such as leasing facilities from other carriers.

Safeguards Against ILEC Anti-Competitive Pricing

In order to prevent anti-competitive pricing by the ILECs, the CRTC imposed a price floor test that requires the ILECs to impute or notionally charge themselves for their own services. The prices ILECs may charge end-users must be sufficient to recover the costs of the ILECs which:

- with respect to essential facilities, must be at least equal to the essential services rates charged to CLECs (i.e., long-run incremental cost plus 25%); and
- with respect to non-essential services, must be at least equal to long-run incremental costs.

The Local Competition Decision requires the ILECs to meet the price floor test in all applications for new local business services and applications proposing explicit or implicit price decreases. The CRTC's price floor test is an important safeguard for CLECs against anti-competitive pricing. However, since the ILECs need not include the mandated 25% markup in their prices for services provided over non-essential facilities, the ILECs will be able to compete on the basis of price when providing these services, as well as on the basis of any other competitive advantages they may have.

Resale of ILEC Services

Prior to the introduction of local competition, customers could only obtain local service from an ILEC or a reseller. A reseller leases services from an ILEC. The leased services are usually Centrex services, which include features either not available, or only available at extra cost, on the ILECs' basic single-line business service. Centrex services are usually available from the ILEC in large quantities and purchased by the reseller at bulk discounts. The reseller then offers these services to end-customers with needs for fewer lines, at price levels close to those an ILEC charges for basic single-line business service, but with additional features included as part of the price.

In the Local Competition Decision, the CRTC required the ILECs to make their tariffed local switched services, both business and residential, available for resale, but not at any kind of mandated discount as had been proposed to the CRTC by some potential new entrants. The CRTC's denial of mandated discounts does not affect current ILEC business services already offered at volume and contract term discounts, such as Centrex services. However, the absence of mandated discounts will likely limit the number of non-facilities-based entrants, such as resellers, into the local switched services market, especially for residential customers.

Contribution

In the Local Competition Decision, the CRTC denied requests by the ILECs to require CLECs to pay contribution charges on local business exchange services as a subsidy source for the cost of providing local residential services. As a result, the only source of subsidy for local residential services remains the contribution that long distance carriers, wireless carriers and long distance resellers pay on switched long distance calls and on direct access lines and on local services used for multi-hop resale, where services are moved from one central office to another. These contribution revenues are pooled within each ILEC's territory and are paid out to the ILECs and CLECs serving residential customers, based on the number of residential network access services they serve and the level of subsidy available in the rate band being served. The Company will not receive any of these revenues so long as it does not provide residential local service.

The current contribution regime is the subject of a proceeding to review the contribution collection mechanism, which currently levies contribution charges on long distance services only, on a per-minute basis, based on network configurations. Submissions were provided to the CTRC on November 30, 1999 and final arguments are due in July 2000. Proposals contained in these submission included an approach based on the revenues of telecommunications service provides, a per-subscriber surcharge and maintaining the current contribution collection mechanism. It is too

early to assess what the outcome will be of this proceedings to revise the contribution regime. However, it is possible that this proceeding will result in additional or increased charges being levied upon the long distance or other services provided by Axxent Inc.

Regulation of CLECs

The CRTC considers CLECs to be non-dominant carriers. As such, they are not subject to the same degree of regulation as ILECs. However, the CRTC requires CLECs to assume certain regulatory obligations, including obtaining CRTC approval of interconnection agreements and tariffs for services that they provide to other carriers. Further, CLECs must provide uninterrupted interconnection arrangements to all other LECs providing services within the same exchange area. This arrangement permits the use of a common telephone number configuration for all end-customers and an integrated network between LECs.

In addition, CLECs must provide equal access, through 1+ dialing, from their end-customers to all long distance providers that offer services in the same territory served by the CLEC, and interconnection to all carriers, including long distance, wireless and other LECs operating in the same exchange. This access must be available at terms, conditions, rates and charges no less favourable than those contained in ILEC tariffs.

CLECs are also required to:

- implement local number portability (“LNP”) which permits an end-customer to move from one LEC to another without changing its telephone number;
- provide emergency (9-1-1) service;
- provide message relay service for the hearing impaired; and
- satisfy various other regulatory requirements designed to protect customers’ privacy and ensure that customers receive adequate service information.

Both traditional wireline and wireless service providers may become CLECs as long as they adhere to the obligations imposed by the CRTC.

In early July 1999, Axxent Inc. formally advised the CRTC that it had satisfied each of the mandated entry obligations and requested that the CRTC certify it as a CLEC eligible to operate in designated local switched service markets. The CRTC issued a letter on August 3, 1999 formally acknowledging that the Company’s operating subsidiary had met all of the CRTC’s requirements to operate as a CLEC.

The Company expects its competitive advantage to be based on pricing flexibility, innovative services, feature packaging and timely response to customer needs. In addition, ILECs, unlike Axxent Inc. and other CLECs, will be constrained in responding to market place changes because of the requirement that they seek CRTC approval for changes to their local service offerings prior to implementation. Unlike CLECs, ILECs are also subject to price cap regulation on their local services, an additional regulatory burden. However, like all carriers, including the ILECs, CLECs are subject to the guidelines established by the *Telecommunications Act* against unjust discrimination and granting undue preferences to any person, including the carrier itself. Axxent Inc. views these restrictions as reasonable and fair and does not believe that they will have a material effect on the Company’s planned operations.

Local Number Portability

The CRTC determined that all LECs should bear their own costs of implementing LNP. LNP is now available in all major cities and will be rolled out in smaller centres, based on demand from CLECs. The requirement to request LNP in smaller centres will not impede the Company’s business plan.

Co-location

In June 1997, the CRTC rendered a decision governing ILEC central office co-location arrangements, which are arrangements permitting Axxent Inc. to interconnect its transmission facilities with those of the ILECs using the most efficient and cost-effective network structure. The CRTC mandated that ILECs provide both physical and virtual co-location arrangements, available at the CLEC's option, under CRTC-approved tariffs and a standard form central office licence agreement. A physical co-location arrangement permits a CLEC to place interconnection equipment for exchange of traffic in the ILEC central office building. Virtual co-location arrangements exchange CLEC and ILEC traffic at a designated point outside the ILEC central office. Any additional dedicated facilities located in the central office are provided by the ILEC to complete the CLEC transmission network.

CLECs are also permitted to enter into cross-connection arrangements with any other co-located CLEC within a central office. CLEC-to-CLEC cross-connection arrangements within an ILEC central office are also important to the Company since they increase network efficiency and afford interconnection options similar to those available to the ILECs.

Co-location arrangements are available on a first-come, first-served basis to CLECs at all central offices. Importantly, the CRTC ruled that mandated co-location is available only to carriers interconnecting with ILECs under the terms of either an agreement or tariff approved by the CRTC. Management believes that the requirement limiting co-location access to carriers creates an additional business opportunity for the Company to resell its transmission capacity for connection at central offices to other telecommunications service providers, including resellers and ISPs, which do not have access to mandated co-location arrangements.

The CRTC established monthly rates for a variety of co-location services, including central office floor space and entrance conduit space, as well as for certain non-recurring charges. Axxent Inc. considers the per square metre rates for floor space and conduit to be generally reasonable. While the ILECs may charge essential facilities rates for some co-location elements, such as service order and application charges, many other charges are based upon costs incurred with no mark-ups, such as construction, site preparation and project management services.

Building Access and Inside Wire

An important issue for the Company is access to its customers' facilities in an impartial and economical manner. Control of these facilities and the location of entry to multi-tenant buildings by organizations with either vested interests in their use or financial interest resulting from their control, could have a material effect on the evolving competitive market place. In other words, restricted access to facilities in multi-tenant locations, which are prevalent in the Company's initial target market areas, could mean restricted access to such markets and slower growth. The CRTC recently issued a decision in which it confirmed its intent to ensure end-customers have access to the local service provider of their choice (the "Building Access Decision"). The Building Access Decision specifically states that provision of local telephone service to a multi-tenant building on an exclusive basis is a violation of the *Telecommunications Act*. The Building Access Decision also specified points of connection between LECs and in-building wire and between in-building wire and the end-customer's premise wire. In conjunction with the Building Access Decision, the CRTC recently approved an industry-developed Code of Conduct setting out guidelines and installation practices to be followed when LECs seek access to multi-tenant buildings. The Building Access Decision and the Code of Conduct are favourable to the Company's method of operating in its chosen market place.

Access to Municipal Rights-of-way

A current proceeding before the CRTC involves a dispute between several carriers and the City of Vancouver with respect to right of the carriers to access the municipal roads and rights-of-way of the City. In the proceeding, the carriers have argued that they have a statutory right to access municipal rights-of-way for the purpose of constructing and operating their transmission facilities without the requirement to provide to the City compensation in the form of rent or other consideration. The City has argued that it has the right to charge rent for the use of its roads and rights-of-way. While the CRTC has stated that its review will be limited to the facts of the Vancouver dispute, it acknowledged that any determination in this proceeding may inform future disputes between carriers and other municipalities. In any

event, any decision rendered by the CRTC with respect to the issue of access to municipal rights-of-way should not affect the operations of Axxent as, under its smart build strategy, it does not and will not, for the most part, require access to municipal roads and rights-of-way.

Price Cap Regulation

In the Price Cap Decision released with the Local Competition Decision, the CRTC adopted a form of rate regulation for the ILECs, other than SaskTel, which will bring most of their local services under a price cap regime. Price cap regulation, which replaces rate-based rate of return regulation, regulates the prices of certain services, rather than the ILECs' return on equity. It is intended to improve ILEC productivity by limiting annual price changes on capped services. On an overall basis, the prices for capped services must change by at least the rate of inflation less a productivity offset of 4.5% set by the CRTC. There are additional constraints applied to individual services and sub-baskets of service.

The CRTC excluded certain of the ILECs' local services, such as calling features, voice mail and call waiting, from the price cap regime and from rate regulation. In addition, the CRTC will continue to regulate the rates of certain local competitor services which are used in the provision of local and long distance services outside the price cap regime. Examples of services included in this category are equal access services and network access services provided to wireless carriers. These services will remain subject to detailed rate regulation and prices will generally be set at the ILECs' cost plus a 25% markup.

The CRTC has recently determined that the ILECs may recover, over a number of years, the startup costs associated with the introduction of local competition, including costs related to local network interconnection and local number portability under the price cap mechanism.

Price cap rate regulation will be in force for an initial four-year period and will be reviewed by the CRTC before the end of that period. The CRTC's review may result in the extension of price cap regulation or the elimination of rate regulation for some or all of the ILECs' local services.

Framework for Regulation of Long Distance Services

The Company plans to offer long distance services as part of its bundled telecommunications package. Long distance competition has been in place in Canada since 1990 for resellers and since 1992 for competitive carriers. Since 1994, the ILECs have been required to provide equal access, which eliminates the need for customers of competitive long distance providers to dial additional digits when placing long distance calls through the competitive carriers.

As discussed above in connection with local services, all long distance service providers must make contribution payments to LECs to fund the provision of local residential telephone service. As a competitive long distance provider of voice services, the Company is obligated to make contribution payments. These payments are made at per minute rates based on long distance voice services the Company provides which originate or terminate on the public switched telephone network in Canada. As discussed above, the method of contribution collection is currently being reviewed by the CRTC with a decision not expected before the end of 2000.

The CRTC has refrained from regulating most long distance services and interexchange private line services provided by the ILECs and all such services offered by their competitors. The ILECs remain subject to rate regulation on private line services on those routes which are not yet subject to sufficient facilities-based competition. The CRTC's decision not to regulate long distance services provided by the ILECs has given them additional pricing flexibility, including the ability to price their services below cost, and, as a result, has greatly enhanced their ability to compete with the Company on the basis of price.

In October 1998, Teleglobe's monopoly over overseas telecommunications services to and from Canada ended, thereby permitting both facilities-based carriers and resellers to compete with Teleglobe for the provision of basic international telecommunications services. In response, the CRTC instituted a licensing regime for service providers

such as Axxent Inc., which provide basic international telecommunications services in Canada. The Company's Class B licence application in respect of such services was issued by the CRTC on November 12, 1999.

Interconnection

In April 1997, the CRTC issued its unbundled rates for equal access decision which unbundles the rates that competitive long distance providers pay to the ILECs for various network components of switched access to long distance services, such as the ability of a long distance provider to connect with the local access networks.

The rates established in this decision are important to the Company's business. First, the Company will be required to pay these rates to the ILECs for origination or termination of long distance traffic at either the toll switch or local end office (known as the "switching and aggregating" rates). The rate for direct connection to the local end office of all of the ILECs which was reduced in a December 1999 decision is \$0.003 per minute, while the rates for access tandem connections range from \$0.004 per minute to \$0.007 per minute, depending on the ILEC. Second, as a CLEC, Axxent Inc. will compete with the ILECs in the provision of switched access to long distance services. Accordingly, Axxent Inc. will price its services to compete with the ILECs' tariffed per minute rates.

In its May 1999 decision regarding the regulatory framework for the Internet, the CRTC acknowledged that a comprehensive review of interconnection and unbundling arrangements was necessary and indicated that it would shortly initiate such a proceeding. The CRTC has since commenced consultations with industry participants regarding these issues.

In a separate development, a U.S.-based DSL provider has recently applied to the CRTC to obtain access to the ILECs' unbundled local loops and central office co-location sites on the same terms and conditions as CLECs. In addition, Bell Canada has applied for approval of a tariff under which it would provide access to its unbundled local loops to resellers using DSL access technology. If granted approval, these applications could create opportunities for additional competition in the high-speed Internet access market from service providers which are not subject to the same restrictions on foreign ownership and control as the CLECs.

Regulation of Wireless Services

The use of radio spectrum to provide wireless telecommunications services is subject to allocation and licensing by Industry Canada under the *Radiocommunication Act* (Canada). Accordingly, should Axxent Inc. decide to own or operate wireless telecommunications facilities to extend the reach of its networks, the Company will be subject to additional licensing and regulation by Industry Canada.

In the near term, the Company does not intend to acquire use of the radio spectrum, but may lease wireless capacity from licensed wireless service providers should attractive opportunities appear. The Company does not require an Industry Canada licence in order to lease capacity from another carrier.

Pay Phone Competition

In June 1998, the CRTC issued a decision opening the local pay phone market to competition. This decision paved the way to pay phone competition by CLECs as well as by parties that are not LECs. The CRTC has decided not to regulate the rates that may be charged by new entrants for pay phone calls, but has imposed a number of safeguards relating to pay phone services that are designed to protect consumers from hidden charges and to facilitate the resolution of complaints. These safeguards must be administered by the LEC which provides the access line to the pay phone supplier. This requirement may create some additional administrative costs should Axxent Inc. provide access service to any competitive pay phone provider.

Foreign Ownership Restrictions

The Company has met all of the foreign ownership requirements of the *Telecommunications Act* and intends that its operating subsidiary will remain Canadian-owned and controlled and eligible to operate as a "Canadian carrier"

for the purposes of the *Telecommunications Act*.

In order to be eligible to operate as a Canadian carrier, the Company's operating subsidiary is required by the *Telecommunications Act* to be a "Canadian-owned and controlled" corporation, incorporated or continued under the laws of Canada or a province of Canada. The Company's operating subsidiary is deemed to be Canadian-owned and controlled if:

- at least 80% of the members of its board of directors are Canadians;
- Canadians own at least 80% of its issued and outstanding voting shares; and
- it is not otherwise controlled in fact by persons that are not Canadian.

A "Canadian" for the purposes of these requirements includes: a Canadian citizen who is ordinarily resident in Canada; a permanent resident of Canada; and corporations in which Canadians beneficially own and control in the aggregate not less than $66\frac{2}{3}\%$ of the issued and outstanding voting shares and which are not otherwise controlled in fact by non-Canadians.

A voting share for purposes of these requirements means a share of any class of shares of a corporation carrying voting rights whatsoever and includes convertible securities and options that are currently exercisable.

All of the outstanding common shares of the Company's operating subsidiary are owned by Axxent Inc. Regulations under the *Telecommunications Act* provide that, in order for a holding company such as Axxent Inc. to be considered Canadian:

- at least $66\frac{2}{3}\%$ of the issued and outstanding voting shares of that company must be owned by Canadians; and
- the company must not otherwise be controlled in fact by non-Canadians.

At least $66\frac{2}{3}\%$ of Axxent Inc.'s Class A voting shares are held by Canadians. The Company's Class B non-voting shares are non-voting shares so the issuance and sale of such shares to non-Canadians would not cause a breach of the provisions of the *Telecommunications Act*. Assuming the exercise of the Note Warrants issued in connection with the 1997 Notes, the exercise of the Special Warrants issued in April, 1999, the conversion of the preferred shares issued in connection with the Pathway acquisition, the exercise of the Rhythms Special Warrant and the exercise of all issued options to purchase Class B non-voting shares, the equity interest of non-Canadian shareholders in the Company would be approximately 23.3% through their holding of Class A voting shares and Class B non-voting shares prior to the Company's initial public offering. See "Principal Shareholders" and "Description of Share Capital".

As indicated above, a Canadian carrier must also not be otherwise controlled by non-Canadians. The term control is defined in the *Telecommunications Act*, and includes "control in fact" which term is not defined; however, in past decisions, the CRTC has considered a number of factors to be relevant to the determination of whether a regulated entity is controlled in fact by non-Canadians, including:

- the election and composition of the board of directors;
- the industry-specific experience (or lack thereof) of the non-Canadian shareholders and Canadian shareholders;
- the ability to appoint senior management, the power to determine policies, operations and strategic decision-making; and
- the percentage of equity interest (whether voting or non-voting) held by non-Canadians.

The capital structure of the Company has been designed to ensure compliance with the Canadian ownership requirements. The Company's Articles provide that the Class A voting shares are convertible into Class B non-voting shares subject to the approval of the board of directors. The Articles further provide that all outstanding Class B non-voting shares will be converted into Class A voting shares if all of the restrictions on the ownership of voting shares, and the control in fact, of the Company by non-Canadians under the *Telecommunications Act* and any other statute applicable to Axxent Inc. which restricts non-Canadian ownership and control are eliminated and non-Canadian ownership and control of the Company is not otherwise restricted or expected to be restricted by law. The regulations under the *Telecommunications Act* provide the Company with the time and ability to rectify ineligibility resulting from insufficient Canadian ownership of voting shares, notwithstanding any provision of the Articles or the Company's by-laws.

These Canadian ownership restrictions may limit the Company's ability to raise additional capital outside of Canada. Further, although management believes that the Company has at all times been in compliance with the relevant legislation, there can be no assurance that a future CRTC determination or events beyond the control of Axxent Inc. will not result in the Company ceasing to comply with the relevant legislation. Should this occur, which, in management's view, is unlikely, the Company's eligibility to operate as a carrier under the *Telecommunications Act* could be jeopardized and the business of the Company could be materially adversely affected. If Axxent Inc. becomes subject to proceedings before or against the CRTC with respect to its compliance with the relevant legislation, the Company could be materially adversely affected, even if it were ultimately successful in such a proceeding.

MANAGEMENT

Directors, Executive Officers and Key Consultants

The following table provides certain information concerning the directors, officers and other key personnel of Axxent Inc.'s operating subsidiary. The Articles provide for a minimum of one and a maximum of 10 directors. Pursuant to a special resolution of the shareholders, the number of directors has been set at nine.

<u>Name and Municipality of Residence</u>	<u>Position</u>
Robert Latham ⁽¹⁾⁽³⁾⁽⁴⁾ <i>Toronto, Ontario</i>	Chief Executive Officer, President and Director
William Young ⁽¹⁾⁽²⁾ <i>Toronto, Ontario</i>	Chairman and Director
Christopher Clinning ⁽¹⁾ <i>Oakville, Ontario</i>	Chief Financial Officer and Secretary
Mahmoud Bargout ⁽⁵⁾ <i>Toronto, Ontario</i>	Senior Vice President, Engineering
Daniel Roy <i>Toronto, Ontario</i>	Chief Information Officer
Roger Abbiss ⁽¹⁾ <i>Toronto, Ontario</i>	Director
Scott Chandler <i>Littleton, Colorado</i>	Director
Stephen Coxford ⁽¹⁾⁽³⁾⁽⁴⁾ <i>Toronto, Ontario</i>	Director
Perry Dellelce ⁽¹⁾⁽³⁾ <i>Toronto, Ontario</i>	Director
William Dodds ⁽¹⁾⁽²⁾⁽⁴⁾ <i>Waterdown, Ontario</i>	Director
David Ferguson ⁽¹⁾⁽³⁾⁽⁴⁾ <i>Toronto, Ontario</i>	Director
James Walker ⁽¹⁾⁽²⁾ <i>Toronto, Ontario</i>	Director
Tom Davis <i>Oakville, Ontario</i>	Marketing Consultant
Ashok Kalle <i>Toronto, Ontario</i>	President, Pathway Internet Division
Steve Kerekes <i>Burlington, Ontario</i>	Marketing Consultant

(1) Holds the same position with Axxent Inc. (the holding company).

(2) Member of the Audit Committee.

(3) Member of the Compensation Committee.

(4) Members of the Executive Committee.

(5) Mr. Bargout has informed the Company that he intends to resign from his current position with the Company effective June 30, 2000. The Company has made an offer of employment to an experienced member of the telecommunications industry who will replace Mr. Bargout on his departure.

In order to meet the requirements of the conditional listing approval of The Toronto Stock Exchange (the "TSE") for the Class B non-voting shares, Axxent Inc. appointed James Walker, an independent director, to its board of directors on November 3, 1999. In addition, the Company has agreed with the TSE to appoint an additional director who meets the independence requirements of the TSE. The Company expects to fulfil this obligation in the near future.

In accordance with the terms of the joint venture agreement with Rhythms NetConnections in respect of Rhythms Canada, Rhythms NetConnections is entitled to designate one nominee for election or appointment to the board of directors of Axxent Inc. for so long as it is the holder of all of the Class B non-voting shares issued upon exercise of the Rhythms Special Warrant. Scott Chandler has been appointed to the board of directors of the Company as a nominee of Rhythms NetConnections.

Biographical Information

Robert Latham. Mr. Latham joined the Company as President and Chief Executive Officer on October 3, 1999. From January 1998 to September 1999, Mr. Latham was the President of ORBCOMM Global L.P. (“ORBCOMM”), a telecommunications company based in Dulles, Virginia. From April 1997 to January 1998, Mr. Latham served as the Executive Vice President of ORBCOMM. From February 1996 to February 1997, Mr. Latham was Managing Director, Telecom for Bell Canada International Management Ltd., U.K. (“BCIM”). From April 1996 until November 1996, Mr. Latham was seconded to Mercury Communications Limited in London England, a facilities-based carrier, as the Managing Director, Commercial Service. Prior to joining BCIM, Mr. Latham spent 28 years with Bell Canada, most recently as Group Vice President, Gateways and Public Telephony. From July 1992 to February 1995, Mr. Latham held the positions of Group Vice President, Business Sales and Services and Group Vice President, Signature Service with responsibility for Bell Canada’s business accounts in Ontario. From 1986 to 1991, Mr. Latham led the development of Bell Cellular as President and Chief Executive Officer. Prior to 1986, Mr. Latham held a variety of positions with Bell Canada including in the areas of Business Development, Customer Services, Regulatory Matters, Cost and Performance and Forecasting and Planning.

William Young. Mr. Young joined the Company in January 1998 as President and Chief Executive Officer. Since October 3, 1999, Mr. Young has served as Chairman. From 1994 to 1997, Mr. Young was President and CEO of Derwing Capital Corp., an investment holding company that invested in and provided consulting services to early stage growth companies. From 1986 to 1994, Mr. Young was the President and CEO of The Hamilton Group Limited, a computer reseller specializing in systems integration. The Hamilton Group Limited was a public company listed on the TSE. Since July 1996 Mr. Young has been a Director for MFP Technology Services Ltd., a leading Canadian provider of financing and technology management software applications listed on the TSE.

Christopher Clinning. Mr. Clinning joined the Company in November 1996 as Vice President, Finance. Mr. Clinning was promoted to Senior Vice President, Finance and Operations in May 1998 and to Chief Financial Officer in March 1999. Prior to joining the Company, from April 1996 to October 1996, Mr. Clinning was a consultant to ISM Information Systems Management Corporation. Mr. Clinning served as Vice President and Controller for TeleZone Corporation, a paging company and personal communications licence applicant, from April 1994 to June 1996. From 1988 to March 1994, he held various positions, including Controller for the Ontario region of ISM Information Systems Management Corporation. Mr. Clinning is a chartered accountant.

Mahmoud Bargout. Mr. Bargout joined the Company in August 1998 as a contract employee. In November 1998, he was hired as Senior Vice President of Engineering. Mr. Bargout brings over 22 years of telecommunications infrastructure and network expertise. In his previous role as Vice President of Engineering for JONOROLA Inc. (“JONOROLA”) from October 1997 to June 1998, he was responsible for overseeing a switching, data and fibre optics network stretching across Canada and the U.S. From 1985 to January 1996, Mr. Bargout held a variety of senior positions with Bell Canada including General Manager – Network Planning. In this capacity, he was responsible for developing and directing corporate strategies for local number portability and local competition network architecture. Mr. Bargout has informed the Company that he intends to resign from his current position with the Company effective June 30, 2000. The Company has made an offer of employment to an experienced member of the telecommunications industry who will replace Mr. Bargout on his departure.

Daniel Roy. Mr. Roy joined the Company in May 1998 as Vice President, Information Systems. Mr. Roy has served as the Company’s Chief Information Officer since December 1999. Mr. Roy has broad experience in the integration of information systems within the telecommunications industry. Mr. Roy held the position of Vice President, Telecommunications and Information Systems for Frontier ConferTech Canada from November 1996 to May 1998. As

a member of Frontier ConferTech's Leadership Group, he was responsible for developing and maintaining their Canadian teleconferencing network, which included voice, video and data. Mr. Roy was responsible for the Information Systems Group which was involved in the development of its next generation conferencing systems. Prior to joining Frontier ConferTech, Mr. Roy was also responsible for the International Telecommunications group with Guardian Insurance Co. of Canada, where he held senior telecommunications and information systems positions from June 1988 to November 1996.

Roger Abbiss. Mr. Abbiss is Axxent Inc.'s founder and has served on the board of directors as its Chairman from October, 1994 to September, 1999. He has worked extensively in the telecommunications industry since 1984 and has, over the last decade, founded three Canadian telecommunications ventures. In October 1992, Mr. Abbiss founded ACCPlus, a direct marketing company for ACC TelEnterprises Inc., a long distance reseller. Prior to founding ACCPlus, in October of 1990, Mr. Abbiss started OnePlus Long Distance Corp., the first switchless reseller of long distance service in Canada. From March 1990 to October 1990, Mr. Abbiss worked for JONOROLA, a long distance reseller, as senior sales executive. From December 1988 to January 1990, he was in partnership with the Lakeview Telephone Corporation, an interconnect company. Mr. Abbiss began his career in sales with Canadian Telecommunications Group., an interconnect company.

Stephen Coxford. Mr. Coxford has been a member of the Company's board of directors since September 1996. Mr. Coxford has been President of Gresham & St. Andrew Inc., an investment holding company, since August 1995 and is one of the Company's early-stage investors. From January 1992 to July 1995, Mr. Coxford was Managing Director of Classic Communications Ltd., a cable communications company serving suburban Toronto, and was President of Classicomm FiberLink Ltd., the competitive access provider affiliate of Classic Communications Ltd. Both companies were sold to Shaw Communications Inc. in 1995. From May 1985 to December 1997 Mr. Coxford was a partner in Smith Lyons, a Toronto law firm.

Scott Chandler. Mr. Chandler has been a member of the Company's board of directors since May 2000. Mr. Chandler has been the Senior Vice President – Global Business Development of Rhythms NetConnections since April 2000. From April 1998 to April 2000, Mr. Chandler served as Rhythms NetConnections' Chief Financial Officer and Business Development Officer. Before joining Rhythms NetConnections, Mr. Chandler served as President and Chief Executive Officer of C-COR.net, a cable television and broadband telecommunications equipment company, from August 1996 to April 1998.

Perry Dellelce. Mr. Dellelce has been a member of the Company's board of directors since September 1997. Mr. Dellelce has been a partner with the law firm Wildeboer Rand Thomson Apps & Dellelce, LLP since February 1993 and practices corporate and securities law. Mr. Dellelce represents several investment dealers and public and private companies. Wildeboer Rand Thomson Apps & Dellelce, LLP has been legal counsel to the Company since February 1996. From July 1997 to January 1998, Mr. Dellelce was the Company's President and Chief Executive Officer.

William Dodds. Mr. Dodds has been a member of the Company's board of directors since September 1996. Mr. Dodds has served as Vice President and Secretary of The Woodbridge Company Limited, an Ontario private investment holding company, since January 1980. Mr. Dodds is also a director of Certicom Corporation, a security encryption corporation listed on the TSE.

David Ferguson. Mr. Ferguson has been a member of the Company's board of directors since July 1999. Mr. Ferguson has served as a Vice President of The Vengrowth Investment Fund Inc., a Canadian venture capital fund, since August 1994. Mr. Ferguson served as a Managing Director of Cohen & Ferguson Translink Inc., a Canadian corporate merger and acquisition firm, from January 1990 to August 1994. Mr. Ferguson also serves on the board of directors of Andaurex Industries Inc. a Canadian engineering firm listed on the Vancouver Stock Exchange and served on the board of directors of Genesis Microchip Inc., a company listed on NASDAQ, from August 1996 to May 1999.

James Walker. Mr. Walker has been a member of the Company's board of directors since November 1999. Mr. Walker is a Managing Director of Savage Walker Capital Inc., a merchant bank, which he co-founded and is funded by, and affiliated with, the Ontario Teachers' Pension Plan Board, one of Canada's largest providers of equity capital.

From 1993 to 1998, Mr. Walker was employed by Gentra Inc. from which he resigned in 1998 as President and Chief Executive Officer.

Tom Davis. Mr. Davis is a principal of KEDA Consulting and was appointed Senior Vice President, Customer Operations of the Company in February 2000. Mr. Davis served as Axxent Corp.'s Senior Vice President of Sales under the Company's agreement with KEDA since 1999. He has over 26 years of telecommunications experience. From September 1996 to February 1999 Mr. Davis was contracted by AT&T Canada Inc. to develop, implement and manage a small business strategy to significantly increase market share and revenue while greatly reducing customer attrition. From January to August 1996, Mr. Davis was involved as a consultant and investor in two small business start-ups as well as providing consulting services to an ISP. From July 1994 to December 1995, Mr. Davis was President and Chief Operating Officer of Cam-Net Communications Inc., a telecommunications reseller, a position he assumed upon the acquisition by Cam-Net of Preferred Telemanagement Inc., a company he co-founded in 1993.

Ashok Kalle. Mr. Kalle is President of Pathway, the Company's Internet division. Mr. Kalle founded Pathway Communications in December 1994. Mr. Kalle spearheaded Pathway's diversification into applications development, e-commerce and network integration. Prior to starting Pathway, Mr. Kalle held the position of Director of Human Resources with Sun Life of Canada from June 1990 to May 1995.

Steve Kerekes. Mr. Kerekes is a principal of KEDA Consulting and since 1999 has served as Axxent Corp.'s Senior Vice President of Marketing under the Company's agreement with KEDA. He has 17 years of telecommunications experience. From September 1996 to February 1999, Mr. Kerekes was contracted, along with Mr. Davis, by AT&T Canada to develop, implement and manage a small business strategy to significantly increase market share and revenue while greatly reducing customer attrition. From January to August 1996, Mr. Kerekes was involved as a consultant and investor in two small business start-ups as well as providing consulting services to an ISP.

Committees of the Board of Directors

The Company's board of directors currently has three committees: an audit committee, a compensation committee and an executive committee.

The audit committee consists of Messrs. James Walker, William Dodds and William Young. The audit committee is responsible for making recommendations concerning the engagement of independent auditors, reviewing with the independent auditors the plans and results of the audit engagement, approving professional services provided by the independent auditors, reviewing the independence of the independent auditors, considering the range of audit and non-audit fees and reviewing the adequacy of all internal accounting controls.

The Company's compensation committee consists of Messrs. Stephen Coxford, Robert Latham, David Ferguson and Perry Dellelce. The compensation committee is responsible for the determination of compensation of the Company's executive officers and consultants and the administration of any employee incentive plans.

The Company's executive committee consists of Messrs. Robert Latham, Stephen Coxford, William Dodds and David Ferguson.

Executive Compensation

The following table sets forth information concerning compensation for services in all capacities paid to the Company's Chief Executive Officer and each the four most highly compensated executive officers of the Company (the "Named Executive Officers").

Summary Compensation Table

<u>Name and Principal Position</u>	<u>Fiscal Year</u>	<u>Annual Compensation</u>		<u>Other Annual Compensation</u>	<u>Long Term Compensation</u>	
		<u>Salary</u>	<u>Bonus⁽¹⁾</u>		<u>Class B non-voting shares Underlying Options</u>	<u>All Other Compensation</u>
Roger Abbiss ⁽²⁾⁽³⁾ Chairman	1999	\$151,185	\$ —	\$222,580	—	—
	1998	126,000	—	—	—	—
	1997	120,750	100,000	—	—	—
William Young ⁽⁴⁾ President and Chief Executive Officer	1999	159,814	100,000	7,800 ⁽⁶⁾	—	—
	1998	112,442 ⁽⁵⁾	100,000	5,525 ⁽⁶⁾	600,000	—
	1997	—	—	—	—	—
Christopher Clinning Chief Financial Officer and Secretary	1999	155,937	75,000	7,800 ⁽⁶⁾	15,000	—
	1998	145,056	72,500	7,800 ⁽⁶⁾	116,667	—
	1997	96,656 ⁽⁷⁾	75,000	2,925 ⁽⁶⁾	35,000	—
Mahmoud Bargout Senior Vice President, Engineering	1999	139,194	45,000	7,150 ⁽⁶⁾	183,333	—
	1998	—	—	—	—	—
	1997	—	—	—	—	—
David Kington Vice President, Business Development	1999	122,915	25,000	7,800 ⁽⁶⁾	8,333	—
	1998	143,932 ⁽⁸⁾	—	7,800 ⁽⁶⁾	50,000	—
	1997	78,658 ⁽⁹⁾	—	4,250 ⁽⁶⁾	35,000	—
Daniel Roy Chief Information Officer	1999	136,782	45,000	7,800 ⁽⁶⁾	25,000	—
	1998	51,283 ⁽¹⁰⁾	—	—	—	—
	1997	—	—	—	—	—

- (1) The bonus refers to the fiscal year to which such payment relates, rather than the year in which such bonus payment was made.
- (2) The compensation listed was paid to Mr. Abbiss through Merit Referral Systems, Inc. under a consulting agreement which remained in effect until June 30, 1999. See “Management – Consulting Agreements”.
- (3) In September 1999 Mr. Abbiss resigned as Chairman of the board of directors.
- (4) Effective October 3, 1999 Mr. Young resigned as President and Chief Executive Officer of Axxent Inc. and became the Chairman of the board of directors.
- (5) Mr. Young commenced employment on January 5, 1998 and earned \$112,442 for the nine months ended September 30, 1998.
- (6) Messrs. Young, Clinning, Bargout, Kington and Roy, received a monthly car allowance of \$650 per month.
- (7) Mr. Clinning commenced employment on November 11, 1996 and earned \$96,656 for the period ended September 30, 1997.
- (8) Includes commissions of \$22,500.
- (9) Mr. Kington commenced employment on January 20, 1997 and earned \$78,658 in salary and commissions for the eight months ended September 30, 1997.
- (10) Mr. Roy commenced employment in May 1998 and earned \$51,283 in salary and commissions for the period ended September 30, 1998.

Stock Option Grants

The following table sets forth information regarding options to purchase Class B non-voting shares granted during fiscal year 1999 to each of the Named Executive Officers.

Option Grants in Fiscal Year 1999

	Individual Grants				
	Securities Under Option/SARs Granted (#)	% of Total Options Granted to Employees in Fiscal 1999	Exercise or Base Price (\$/Share)⁽¹⁾	Market Value of Securities Underlying Options/SARs on the Date of the Grant (\$/Share)	Expiration Date
Roger Abbiss	—	—	—	—	—
William Young	—	—	—	—	—
Christopher Clinning	15,000	0.4%	12.00	12.00	August 1, 2004
Mahmoud Bargout	166,667	4.9%	3.00	3.00	October 29, 2003
	16,667	0.4%	12.00	12.00	August 1, 2004
David Kington	8,333	0.2%	12.00	12.00	August 1, 2004
Daniel Roy	25,000	0.7%	12.00	12.00	August 1, 2004

(1) The exercise price on the date of grant was equal to 100% of the estimated fair market value of the shares on the date of grant.

Option Exercises and Option Year-End Value Table

No options were exercised during fiscal year 1999 by any of the Named Executive Officers. The following table sets forth information regarding the number and year-end value of unexercised options to purchase Class B non-voting shares held at September 30, 1999 by each of the Named Executive Officers.

Fiscal 1999 Year-End Option Values

Name	Shares Acquired On Exercise (#)	Value Realized (\$)	Number of Securities Underlying Unexercised Options at September 30, 1999		Value of Unexercised “In-the-Money” Options at September 30, 1999
			Exercisable/Unexercisable		Exercisable/Unexercisable (\$)⁽¹⁾
Roger Abbiss	0	0	0	0	—
William J. Young	0	0	300,000	300,000	2,700,000/2,700,000
Christopher Clinning	0	0	84,583	82,084	798,747/616,256
Mahmoud Bargout	0	0	41,667	141,667	375,003/1,125,000
David Kington	0	0	51,250	42,083	498,750/316,250
Daniel Roy	0	0	33,333	58,334	299,997/300,006

(1) Options are “in-the-money” if the fair market value of the underlying shares exceeds the exercise price of the options. The value of unexercised in the money options in September, 1999 is calculated based on the initial public price of \$12.00 per share.

Indebtedness of Directors and Executive Officers

None of the Company’s directors, executive officers or senior officers, nor any associate of such director, executive officer or senior officer has, at any time since the beginning of fiscal 1998, been indebted to the Company or any of its subsidiaries except that Mr. Robert Latham has borrowed \$75,000 from the Company pursuant to the terms of his employment contract. Under the terms of a promissory note in favour of Axxent Corp., Mr. Latham is required to repay the principal on or before April 11, 2001. In addition, none of the indebtedness of these individuals to another

entity has been the subject of a guarantee, support agreement, letter of credit or similar arrangement or understanding of Axxent Inc. or any of its subsidiaries.

Directors and Employee Stock Options

The following table sets forth information as of April 30, 2000 concerning outstanding options granted to the Company's executive officers and key consultants, non-executive directors, employees and others.

	Number	Optioned Class B Non-Voting Shares	Exercise Price⁽¹⁾	Expiration Date
Officers and key consultants	19	2,697,933	\$1.50 to \$16.00	February 20, 2002 to April 5, 2005
Non-executive directors	7	326,667	\$1.50 to \$12.00	January 31, 2003 to November 11, 2004
Employees	640	1,092,108	\$1.50 to \$25.00	February 20, 2003 to April 30, 2005
Others	0	<u>0</u>	—	—
TOTAL		<u>4,116,708</u>		

(1) The exercise price equals the fair market value of the Class B non-voting shares, as determined by the board of directors on the date of the grant.

Share Option Plan

The Company's share option plan was transferred from its operating subsidiary to Axxent Inc. on July 29, 1999. There are 5,000,000 Class B non-voting shares reserved for issuance under the plan. Eligible persons under the plan are the directors, officers, employees and key contributors of the Company. The board of directors determines the exercise price for options granted under the plan, which must not be less than the fair market value at the time of the grant, the term of the options and the vesting schedule, if any.

The plan is administered by the board of directors, which determines the individuals who are to receive options, the time periods during which the options may be exercised, the number of shares issuable upon the exercise of each option and the option exercise price which may not be less than the closing price of the Class B non-voting shares on the TSE on the last trading day preceding the date on which the grant of the option is approved by the board of directors. In addition, a participant may, rather than exercise options which he or she is entitled to exercise, elect in lieu of receiving the Class B non-voting shares to which the participant would have been entitled on exercise of such options, receive instead the number of Class B non-voting shares which, when multiplied by the fair value per share, is equal to the product of the number of Class B non-voting shares the participant would be entitled to receive on exercise of such options times the difference between the fair value and the exercise price per Class B non-voting share. As of April 30, 2000, 4,116,708 options to purchase Class B non-voting shares were outstanding under the plan, and 883,292 Class B non-voting shares were available for future option grants.

Axxent Inc. has also implemented an employee ownership plan under which all of the Company's full-time employees are granted options to purchase Class B non-voting shares upon commencement of employment. The options have been granted under the share option plan.

Retirement Savings Plan

The Company implemented a group retirement savings plan on March 31, 1998. Under the plan, Axxent Inc. contributes 2% of each full-time employee's salary after three months of employment. The Company also matches 50% of an employee's contribution up to an additional 1% of the employee's salary.

Executive Employment Contracts

The Company has employment agreements or remuneration arrangements with all of its executive officers. Each agreement or arrangement provides for salary, benefits, bonuses and incentive stock option grants for the

executive officer, and for compensation if his or her employment is terminated.

Consulting Agreements

Axxent Inc. has a consulting agreement with KEDA Consulting Corp. (“KEDA”) under which KEDA will provide Axxent Inc. with the consulting services of Tom Davis and Steve Kerekes for the sales and marketing of the Company’s products and services. Messrs. Kerekes and Davis are fulfilling the roles of Senior Vice President, Marketing and Senior Vice President, Sales, respectively. The Company has agreed to pay KEDA a fee of \$30,000 per month during the term of the agreement plus an extraordinary fee of \$10,000 per month if the number of total lines subscribed for during such month exceeds 3,000. In addition, the Company has issued 83,333 options to purchase Class B non-voting shares under the Company’s share option plan at an exercise price of \$6.00 per share to each of Tom Davis and Steve Kerekes. These options expire on May 31, 2004. A further 8,333 options were issued to each of Messrs. Davis and Kerekes on September 16, 1999, each option to purchase one Class B non-voting share at an exercise price of \$12.00. These options vest equally over a three year period beginning September 16, 2000. A further 83,333 options have been issued to each of Messrs. Davis and Kerekes at an exercise price of \$12.00. These options will expire on November 4, 2005.

Compensation of Directors

The Company does not currently pay any cash compensation to directors for serving on the board, but does reimburse directors for out-of-pocket expenses, if any, for attending board and committee meetings. In addition, on November 4, 1999, each non-management director, with the exception of Mr. James Walker, was granted options to purchase 25,000 Class B non-voting shares at a price of \$12.00 per share. Mr. Walker was granted options to purchase 10,000 Class B non-voting shares at a price of \$12.00 per share upon election to the board and additional options to purchase 15,000 Class B non-voting shares on November 4, 1999. Non-management directors were also granted options to purchase an additional 5,000 Class B non-voting shares at a price of \$12.00 (to a maximum of 10,000 Class B non-voting shares) for each committee of the board of directors on which such director serves.

RELATED PARTY TRANSACTIONS

Gian D'ornellas was a member of the Company's board of directors from March 1997 to September 1997. In addition, Mr. D'ornellas' consulting service, Cinemedia, acted as the Company's consultant and received fees for these services. Mr. D'ornellas was granted an aggregate of 16,667 options to purchase Class B non-voting shares exercisable at a price of \$2.13 per share. All of the options have vested and expire in 2002.

In September 1996, an equity investment of \$2.5 million was completed with a group of three investors, who subsequently invested an additional \$2.5 million in January and February 1997. Stephen Coxford, a member of the Company's board of directors, was the principal of one of these equity investors. William Dodds, another member of the Company's board of directors, is a representative of another of these investors. A former member of the Company's board of directors, Raymond Doucet, is the principal of the third investor. Those same investors joined with the principals of 956872 Ontario Ltd. to provide Axxent Inc. with a \$6.1 million credit facility in May 1997.

In connection with the September 1996 equity investment, the Company's operating subsidiary became a party to a shareholders agreement with some of its shareholders. Upon the closing of the Special Warrant financing in April 1999, this shareholders agreement was terminated in accordance with its terms.

In 1996, the Company entered into a consulting agreement with Merit Referral Systems, Inc. ("Merit Referral Systems") which is owned and operated by Roger Abbiss, who is a principal shareholder of the Company. The consulting agreement was amended in July 1997 and, on June 30, 1999, was terminated at the mutual agreement of the parties. Merit Referral Systems was paid a severance payment of \$222,580 in connection with the termination of the agreement.

Roger Abbiss, a principal shareholder of the Company, sold 375,000 Special Warrants for gross proceeds of \$750,000 in connection with the April 1999 Special Warrant offering. Each three Special Warrants were exercised, for no additional consideration, for one Class A voting share.

Stephen Coxford, who is a member of the board of directors, has been paid fees for consulting services rendered to the Company's operating subsidiary.

Perry Dellelce, who is a member of the board of directors, is a partner of Wildeboer Rand Thomson Apps & Dellelce, LLP, which has rendered and continues to render legal services to the Company. In addition, Mr. Dellelce was the President and Chief Executive Officer of the Company from July 1997 to January 1998. As partial consideration for these services, Mr. Dellelce was granted an aggregate of 116,667 options to purchase Class B non-voting shares of which 83,334 options are exercisable at a price of \$1.50 per share and 33,333 options are exercisable at a price of \$3.00 per share. All of Mr. Dellelce's options expire in 2003.

David Ferguson, who is a member of the board of directors, is the portfolio manager for The Vengrowth Investment Fund Inc., which purchased 3,000,000 Special Warrants exercisable for 1,000,000 Class A voting shares in April 1999.

Robert Latham, the Chief Executive Officer, President and a director of Axxent Inc., was lent money by Axxent Corp. in accordance with the terms of his employment agreement. Mr. Latham's indebtedness is evidenced by a promissory note dated April 11, 2000 in the principal amount of \$75,000. The promissory note is to mature on April 11, 2001, at which time any unpaid principal amount shall bear interest at a variable rate of interest per annum equal to 2% above the per annum prime rate of the Toronto-Dominion Bank.

PRINCIPAL SHAREHOLDERS

The following table sets forth certain information regarding the beneficial ownership of Class A voting shares as at the date of this prospectus and as adjusted to reflect the issuance of Class B non-voting shares upon exercise of the Special Warrants with respect to each person known by the Company to own beneficially or of record, directly or indirectly, or exercise control or direction over, 10% or more of the Class A voting shares.

Name and Municipality of Residence	Designation of Class	Type of Ownership	Number and Percentage of Class before the Offering	Number and Percentage of Class after giving effect to the Offering
Peter Thomson	Class A voting shares	Indirect	3,393,306 ⁽¹⁾ (48.51%)	3,393,306 (48.51%)
Toronto, Ontario				
Stephen Coxford	Class A voting shares	Indirect and Beneficial	1,100,000 ⁽²⁾ (15.35%)	1,100,000 (15.35%)
Toronto, Ontario				
Vengrowth Investment Fund Inc.	Class A voting shares	Direct	1,000,000 (14.30%)	1,000,000 (14.30%)
Toronto, Ontario				

(1) The Class A voting shares of Mr. Thomson are held by two companies: Undercurrent Holdings Limited as to 1,393,306 Class A voting shares and Sahara Corporation as to 2,000,000 Class A voting shares.

(2) Mr. Coxford holds 26,002 Class A voting shares in his Registered Retirement Savings Plan . The balance of the Class A voting shares are held by Gresham & St. Andrew Inc.

After giving effect to the conversion of the Special Warrants and the Preferred Shares, the officers and directors of the Company will own, directly and indirectly, an aggregate of 73.35% of the outstanding Class A voting shares and 3.88% of the Class B non-voting shares.

CAPITAL REORGANIZATIONS

On October 27, 1999, the Company completed a reorganization of its issued and outstanding share capital. Under such reorganization, the outstanding Class A voting shares, Class B non-voting shares and options to purchase Class B non-voting shares were consolidated on a three-for-one basis.

Pursuant to the May 2000 consent solicitation, the Company has agreed with the holders of the 1997 Notes that it will effect a capital reorganization immediately prior to the filing of a (final) prospectus to qualify, among other things, the distribution of the Class B non-voting shares issuable upon conversion of the Series 3 preferred shares. Pursuant to the proposed capital reorganization, the Company will acquire from any holders of the Note Warrants requesting it to do so, all but not less than all of the Note Warrants held by such holder in exchange for an equal number of Series 3 preferred shares. Each Series 3 preferred share is convertible, upon payment of \$0.03 per share, for one Class B non-voting share. See “Certain Indebtedness of the Company – 1997 Notes”.

DESCRIPTION OF SHARE CAPITAL

The authorized capital of the Company consists of an unlimited number of Class A voting shares, an unlimited number of Class B non-voting shares and an unlimited number of preferred shares issuable in series. At March 31, 2000, there were issued and outstanding 7,000,803 Class A voting shares and 19,375,502 Class B non-voting shares.

Class A voting shares and Class B non-voting shares

Other than with respect to voting rights and conversion rights, the Class A voting shares and the Class B non-voting shares have identical rights.

Dividends. Each Class A voting share and Class B non-voting share is, subject to the rights of the holders of any preferred shares, entitled to receive dividends in an identical amount at the same time and in the same form as determined by the Company's board of directors without distinction or preference among or between these classes.

Voting. The holders of Class A voting shares are entitled to receive notice of any meeting of shareholders of Axxent Inc. and to attend and vote thereat as a single class on all matters to be voted on by the shareholders of Axxent Inc. except in the case of a meeting where only the holders of shares of one class or of a particular series are entitled to vote separately under the *Business Corporations Act* or the Articles. The holders of Class A voting shares are entitled to elect all of the members of the Company's board of directors. The Class A voting shares carry one vote per share.

The holders of Class B non-voting shares are not entitled to vote at any meeting of shareholders of Axxent Inc. except as prescribed by law. The holders of Class B non-voting shares are entitled to receive notice of and attend meetings of holders of Class A voting shares of Axxent Inc.. To the extent the holders of Class B non-voting shares are entitled to vote on any matter, each Class B non-voting share carries one vote per share.

As a result, without the approval of the holders of the Class B non-voting shares, holders of the Class A voting shares will be able, subject to the *Business Corporations Act* and the Canadian provincial securities laws and regulatory policies, to:

- amend the Company's Articles and by-laws, except in certain circumstances where the rights and conditions attaching to the Class B non-voting shares would be adversely affected;
- effect a sale, lease or exchange of all or substantially all of the Company's property other than in the ordinary course of business except in certain circumstances where the proposed transactions would affect the Class B non-voting shares in a manner different from the Class A voting shares affected;
- defeat any takeover attempt;
- elect all of the Company's board of directors; and
- otherwise control the outcome of virtually all matters submitted to a general shareholder vote.

Liquidation and Other Rights. In the event of the liquidation or dissolution of the Company or any other distribution of assets among the shareholders of the Company for the purpose of winding up its affairs, whether voluntary or involuntary, the holders of Class A voting shares and Class B non-voting shares will be entitled, subject to the rights of the holders of any preferred shares, to participate equally on a share-for-share basis in the remaining property and assets of Axxent Inc. available for distribution to its shareholders without preference or distinction.

The Class A voting shares and the Class B non-voting shares are not by their terms redeemable and holders thereof have no pre-emptive or subscription rights to purchase any securities of the Company.

Statutory Rights. Holders of the Class A voting shares and the Class B non-voting shares are entitled to those statutory rights provided to shareholders under the *Business Corporations Act*, which rights include, but are not limited to:

- the right to examine corporate records during usual business hours;
- the right to obtain a shareholder list if certain preconditions in the *Business Corporations Act* are satisfied;
- the right to have comparative financial statements presented at every annual meeting; and
- the right to institute certain remedial proceedings provided for in the *Business Corporations Act* including an application to a court for leave to bring an action in the name of the Company.

Subdivision and Consolidation. In the event that the Class A voting shares or the Class B non-voting shares are at any time subdivided, consolidated or otherwise reclassified or exchanged for the shares of another class, except as a result of the exercise of conversion rights, the rights, privileges and restrictions attached to the shares of the other classes will be amended at the same time so as to preserve the rights conferred by the Articles on each class in relation to the other classes.

Transfer. There are no restrictions on the transfer of the Class B non-voting shares except the constrained share provisions contained in the Articles, the Canadian ownership and control requirements of the *Telecommunications Act* and the regulations thereunder, together with any other foreign ownership restrictions that might ultimately apply to the Company (for example, those enacted under the *Broadcasting Act* (Canada) in the event that the Company came to hold cable assets).

Conversion Privileges. Each Class A voting share may, subject to the approval of the Company's board of directors, be converted into one Class B non-voting share at the option of the holder.

All outstanding Class B non-voting shares will be converted into Class A voting shares if all of the restrictions on the ownership of the Company's Class A voting shares, and the control in fact, by non-Canadians under the *Telecommunications Act* and any other statute applicable to the Company which restricts non-Canadian ownership and control, are eliminated and non-Canadian ownership and control of the Company is not otherwise restricted or expected to be restricted by law.

Coattail Provisions

Under the terms of the Articles, the holders of Class B non-voting shares have been provided with specific rights in the event that a take-over bid is made for the Class A voting shares. In general, these provisions are intended to ensure that the holders of the Class B non-voting shares will have the right to participate in a take-over bid for the Class A voting shares. A take-over bid, generally defined, is an offer to acquire outstanding equity or voting shares by an offeror, who after the bid, would own more than 20% of the shares of the class which is subject to the bid. If a take-over bid is made for the Class A voting shares and a similar offer is not made for the Class B non-voting shares, then the holders of the Class B non-voting shares will have the right to convert their shares into Class A voting shares. The conversion right will not, however, be triggered where holders of more than 50% of the Class A voting shares commit not to tender to the bid.

An election by a holder of Class B non-voting shares to convert his shares into Class A voting shares will be an irrevocable election by such holder to deposit his Class A voting shares into the take-over bid, subject to such holder's right under applicable securities legislation to subsequently withdraw such shares. In the event that the take-over bid is not completed or all of the Class A voting shares that have been tendered as a result of a conversion of the Class B non-voting shares are not converted or withdrawn, the Class A voting shares not taken up under the take-over bid will be automatically converted back to Class B non-voting shares and returned to the holder.

Preferred Shares

Axxent Inc.'s preferred shares may be issued in one or more series, without further approval of the shareholders, upon the filing of articles of amendment. The board of directors may fix the number of shares that is to comprise each series and the designation, rights, privileges, restrictions, conditions and other provisions for the preferred shares of such series, including dividend terms and priority over any of the Company's shares ranking junior to the preferred shares for purposes of dividends and distributions of asset upon liquidation or otherwise. The preferred shares are entitled to preference over any other shares of Axxent Inc. ranking junior to the preferred shares with respect to the payment of dividends and with respect to priority in the event of a distribution upon liquidation.

The preferred shares of each series rank on a parity with the preferred shares of every other series with respect to the payment of dividends, and with respect to priority in the event of a distribution upon liquidation. With the exception of the right to vote on an amendment to the provisions of the Articles relating to the preferred shares or as required by law, the holders of preferred shares will have no voting rights as a class. The holders of preferred shares are

not entitled to vote separately as a class or as a series and are not entitled to dissent on a proposal to amend the Articles, to change any maximum number of authorized preferred shares or to increase any maximum number of preferred shares of the class or series of a class having rights or privileges equal or superior to the preferred shares, to effect an exchange, reclassification or cancellation of the preferred shares, or to create a new class or series of a class of preferred shares equal or superior to the preferred shares. At any meeting of the holders of the preferred shares at which holders of the preferred shares are entitled to vote, each holder of preferred shares is entitled to one vote in respect of each preferred share held by such holder. In addition, holders of preferred shares are entitled to the statutory rights under the *Business Corporation Act* described above.

Series 3 Preferred Shares

The Preferred Shares will be issued to any holder of Note Warrants who wished to exchange such Note Warrants, on a one-for-one basis, for Series 3 preferred shares. There are currently 7,465,250 Note Warrants outstanding. The Series 3 preferred shares will not receive dividends and, except as otherwise provided in the *Business Corporations Act*, the holders of the Series 3 preferred shares will not be entitled to vote at any meetings of the shareholders of the Company. The holders of the Series 3 preferred shares will have the right to convert each Series 3 preferred share into one Class B non-voting share on payment of \$0.03 per share. The Company has agreed with the holders of the 1997 Notes to use its commercially reasonable best efforts to qualify the distribution in Ontario of the Class B non-voting shares issuable upon conversion of the Series 3 preferred shares on or before June 30, 2000.

Upon the issuance of a receipt from the Ontario Securities Commission for a final prospectus qualifying the distribution of the Class B non-voting shares to be issued upon conversion of the Series 3 preferred shares, the rights of the holders of the Series 3 preferred shares then outstanding to convert their Series 3 preferred shares will be deemed to have been fully exercised and the registered holders will be deemed to have become holders of Class B non-voting shares. See “Description of Certain Indebtedness – 1997 Notes”.

Special Warrants

On March 28, 2000, the Company issued 10,000,000 Special Warrants pursuant to the terms of an underwriting agreement with Griffiths McBurney & Partners, CIBC World Markets Inc., Credit Suisse First Boston Securities Canada Inc., Scotia Capital Inc. and Yorkton Securities Inc. Each Special Warrant is exercisable, without payment of any additional consideration, for one Class B non-voting share. The Special Warrants are exercisable until, and will be deemed to be exercised without any further act on the part of the holder, on the day which is the earlier of:

- the sixth business day after a receipt is issued in the province in which the holder of Special Warrants resides for the final prospectus qualifying the issuance of the shares to be issued upon exercise of the Special Warrants; and
- 4:59 (Toronto time) on March 28, 2001.

In the event that the Company has not received a receipt for a final prospectus from the securities regulatory authority in each province in Canada where a holder of Special Warrants resides by July 31, 2000, each Special Warrant exercised after such date will entitle the holder thereof to 1.03 Class B non-voting shares upon exercise.

Pathway Special Warrants

On February 11, 2000, the Company issued 33,333 Pathway Special Warrants to the vendors of the shares of Pathway Communications as part of the deferred consideration contemplated under the share purchase agreement. Each Pathway Special Warrant is exercisable, for no additional consideration, into one Class B non-voting share.

1997 Note Warrants

On December 31, 1997, the operating subsidiary of the Company issued and sold units, comprised of an aggregate of US \$30.0 million plus \$7.2 million of senior notes (the “1997 Notes”) and 7,465,250 Note Warrants. Three

Note Warrants entitle the holder to acquire one common share in the capital of the operating subsidiary of the Company at a purchase price of \$0.03 per share and may be exercised at any time on or before December 30, 2004.

The Company has agreed with the holders of the 1997 Notes to acquire from any holder requesting to do so all but not less than all of the Note Warrants held by such holders in exchange for Series 3 preferred shares.

CTRA Warrants

In connection with the acquisition of CTRA, the Company issued CTRA Warrants to purchase an aggregate of 416,667 Class B non-voting shares at an exercise price of \$6.00 per Class B non-voting share. The CTRA Warrants are exercisable until June 17, 2004.

Registration Rights

The Company is a party to a registration rights agreement dated December 31, 1997, as amended, with the holders of the Note Warrants issued in connection with the 1997 Notes. The registration rights agreement provides that each time Axxent Inc. proposes to file a prospectus or registration statement with securities regulatory authorities in Canada or the U.S., the Company is obligated to offer each of the warrant holders the opportunity to qualify the conversion of their Note Warrants, sell their shares under a secondary offering or register such number of their shares as each such holder may request. The Company is to use its commercially reasonable best efforts to cause the managing underwriter or underwriters of any proposed underwritten public offering to permit the shares to be issued upon exercise of the Note Warrants to be included on the same terms and conditions. The Company has also agreed that in the event Axxent Inc. completes an initial public offering in the U.S., it shall use its commercially reasonable best efforts to subsequently become eligible to use the shelf registration system in the U.S. The Note Warrants will not be qualified under this offering.

Under the terms of the Pathway purchase agreement, the Company has agreed to use its commercially reasonable best efforts to qualify the distribution in Ontario of the Class B non-voting shares to be issued upon exercise of the Pathway Special Warrants. In addition, pursuant to the terms of the May 2000 consent solicitation, the Company has agreed to use its commercially reasonable best efforts to qualify the distribution of the Class B non-voting shares to be issued upon conversion of the Series 3 preferred shares on or before June 30, 2000.

Under the terms of the EDI Communications purchase agreement, the Company has agreed to use its commercial efforts to make an application to, and obtain and order from, the Ontario Securities Commission that reduces the applicable hold period under section 72(5) of the *Securities Act* (Ontario) in respect of the Class B non-voting shares issued by the Company as partial consideration pursuant to the agreement. Such application is to request that the Class B non-voting shares issued in connection with the acquisition of EDI Communications become freely tradeable upon the qualifying and filing of a (final) prospectus of the Company qualifying, among other things, the issuance of the Class B non-voting shares upon exercise of the Special Warrants.

Restrictions on Non-Canadian Ownership and Control

The Articles of the Company provide that Axxent Inc. may, in connection with the issuance or transfer of ownership of any of the shares of the Company, take any action or refuse to take any action to the extent necessary to ensure that the operating subsidiary of the Company is and continues to be eligible to operate as a telecommunications common carrier under the *Telecommunications Act*.

DESCRIPTION OF CERTAIN INDEBTEDNESS

1997 Notes

On December 31, 1997, the Company's operating subsidiary issued and sold units, comprised of an aggregate of US \$30.0 million plus \$7.2 million of senior notes (the "1997 Notes") and 7,465,250 Note Warrants. The aggregate

purchase price of the units was US \$35.0 million. Each three Note Warrants entitle the holder to acquire one common share in the capital of the Company's operating subsidiary at a purchase price of \$0.03 per share. The 1997 Notes will mature on December 30, 2004, and bear interest at 15% per annum. Interest on the 1997 Notes is payable semi-annually on December 15 and June 15 of each calendar year, with an option to issue payment in kind notes in lieu of cash for the first three years of the term of the 1997 Notes. On December 31, 1998, June 30, 1999 and December 31, 1999, the Company's operating subsidiary issued an aggregate of US \$4.7 million, \$1.1 million and \$2.6 million additional senior notes in lieu of interest payable on these dates.

The 1997 Notes are redeemable at the option of the Company, in whole or in part, at any time at specified redemption prices and may be subject to mandatory redemption upon a change of control the Company.

The 1997 Notes were issued and sold under a securities purchase agreement dated as of December 31, 1997. The securities purchase agreement contains covenants which restrict the ability of the Company's operating subsidiary to:

- incur additional indebtedness and issue preferred shares;
- pay dividends or make distributions on share capital;
- make other restricted payments;
- enter into sale-leaseback transactions;
- incur liens or encumbrances;
- cause restrictions to exist on the ability of restricted subsidiaries to pay dividends or make distributions in respect of their share capital;
- issue and sell shares of restricted subsidiaries;
- enter into transactions with affiliates;
- sell assets; or
- amalgamate, consolidate, merge or sell or otherwise dispose of all or substantially all of its property and assets.

The securities purchase agreement does not contain any financial ratios which the Company's operating subsidiary must maintain.

The Note Warrants were issued under a warrant agreement dated as of December 31, 1997. The Note Warrants may be exercised at any time on or before December 30, 2004.

Under the terms of an April 1999 consent solicitation, the Company received the consent of the holders of the 1997 Notes and Note Warrants to certain amendments to the securities purchase agreement and warrant agreement. Such amendments permitted:

- the April 1999 reorganization of the Company and the creation of a holding company structure; and
- the incurrence of indebtedness for additional vendor financing for the acquisition of assets and equipment, limited to three times the funded equity of the Company.

In addition, the consent also obligated the Company, at the holding company level, to assume the obligations of its operating subsidiary in the tag-along agreement and registration rights agreement, each dated as of December 31,

1997. Under the tag-along agreement, if one of the shareholders who is a party to this agreement has already sold or by making a proposed sale to a third party, would have sold in the aggregate more than 25% of the shares held by such shareholder as of September 16, 1996 and such shareholder wishes to sell additional shares, such shareholder must give each warrant holder the right to sell a proportionate amount of the shares issuable upon exercise of the Note Warrants on the same terms and conditions.

In December, 1999, the holders of the 1997 Notes consented to the Company executing the Rhythms Joint Venture Agreement and completing the purchase of U.S. \$100 in voting Class A shares and up to U.S. \$10.0 million of preferred shares in the capital of Rhythms Canada.

Under the terms of a May 2000 consent solicitation, the Company received the consent of the holders of the 1997 Notes to certain amendments to the securities purchase agreement and warrant agreement. Such amendments included:

- the revision of certain covenants of the Company and its operating subsidiary to permit Axxent Inc. to invest up to U.S. \$50.0 million in Rhythms Canada, whether by purchase of assets from Rhythms Canada, purchase of Class A shares or preferred shares, capital contribution, loan, advance or guarantee of indebtedness of Rhythms Canada;
- the revision of certain covenants of the Company and its operating subsidiary to permit Axxent Inc. to incur indebtedness in connection with vendor financing on behalf of Rhythms Canada and to secure indebtedness incurred by Rhythms Canada as contemplated by the joint venture agreement provided that the total indebtedness of the Company or Rhythms Canada held by vendors of the Company, Rhythms Canada or any of the Company's subsidiaries in the aggregate amount does not exceed the greater of (i) \$15,000,000 and (ii) an amount, which when added to all other indebtedness of the Company and JVCO, does not exceed three times the funded equity of the Company provided that only 50% of any indebtedness incurred directly by Rhythms Canada and guaranteed by the Company and Rhythms NetConnections or incurred by the Company and guaranteed by Rhythms Canada shall be included in such calculations; and
- the revision of certain covenants of the Company and its operating subsidiary to permit Axxent Corp. to lease or transfer certain assets to Rhythms Canada as contemplated by the joint venture agreement.

Under the terms of the May 2000 consent solicitation, the holders of the 1997 Notes also agreed to amend the April 1997 consent solicitation to provide that Axxent Inc. shall be permitted to guarantee the obligations of Axxent Corp. under a credit facility provided that the recourse against Axxent Inc. for such guarantee shall be limited to a pledge of securities of Axxent Corp. held by Axxent Inc.

In addition, pursuant to the May 2000 consent solicitation, the Company agreed to acquire from any holder of Note Warrants requesting to do so, all but not less than all of the Note Warrants held by such holders in exchange for Series 3 preferred shares. Each Series 3 preferred share will be convertible for one Class B non-voting share upon payment of \$0.03 per share. The Company has agreed to use its commercially reasonable best efforts to qualify in Ontario the distribution of the Class B non-voting shares issuable upon conversion of the Series 3 preferred shares on or before June 30, 2000.

Nortel Credit Facility

The Company had previously signed a commitment letter with Nortel which contemplated that Nortel, as agent and together with one or more Canadian chartered banks, financial institutions or other lenders, would provide, Axxent Inc.'s operating subsidiary with a secured vendor financing facility of up to \$100.0 million. As a result of the completion of the Special Warrant offering on March 28, 2000, the Company allowed the Nortel commitment letter to expire on March 31, 2000. The Company is currently in discussions with Nortel to explore financing alternatives.

PRIOR SALES

Other than the issuances of the Special Warrants by the Company, the following are the only transactions involving the sale of securities by the Company during the 12-month period ended March 31, 2000.

- On March 23, 2000, the Company completed the acquisition of all the outstanding shares of EDI Communications, an Ontario based company specializing in data network provisioning, including data network design, implementation and operations, for small and medium-sized businesses. As consideration for the transaction, Axxent Inc. issued 210,938 Class B non-voting shares at closing. In addition, Axxent Inc. may be required to issue up to an additional \$5.65 million in Class B non-voting shares if certain performance targets are met. See “Business of the Company – Acquisitions”.
- On February 11, 2000, the Company issued the Pathway Special Warrants as partial consideration in connection with the acquisition of all of the issued and outstanding shares of Pathway. See “Business of the Company – Acquisitions”.
- On October 28, 1999 the Company filed a (final) prospectus in all provinces of Canada qualifying the issuance and sale, by way of initial public offering, of 8,400,000 Class B non-voting shares. This offering closed on November 4, 1999. On December 22, 1999, the Company issued and sold 1,260,000 Class B non-voting shares upon the exercise of an over-allotment option granted to the underwriters in connection with the initial public offering.
- On October 27, 1999, the Company issued the Rhythms Special Warrant in accordance with the terms of a memorandum of understanding between Rhythms NetConnections and the Company’s operating subsidiary. The Rhythms Special Warrant was exercised, for no additional consideration, for 763,680 Class B non-voting shares in December 1999.
- On July 29, 1999, the Company acquired all of the issued and outstanding shares of Pathway, a Toronto-based ISP that also provides, network integration and other Internet-related services. Axxent Inc. acquired Pathway for consideration at closing, consisting of a payment of \$3.5 million cash and the issuance of Series 1 and Series 2 preferred shares which were converted into an aggregate of 416,667 Class B non-voting shares. In addition, the Pathway transaction provided for performance-based compensation of \$500,000 cash and special warrants, including the Pathway Special Warrants, exercisable, at no additional consideration, for 83,333 Class B non-voting shares valued at \$500,000 based on Pathway meeting certain performance goals. See “Business of the Company – Acquisitions”.
- On June 17, 1999, the Company acquired all of the issued and outstanding shares of CTRA through the acquisition of all of the issued and outstanding shares of Oakbrook Communications Inc. The CTRA purchase agreement provided for aggregate cash consideration of \$500,000 and the issuance of the CTRA Warrants to purchase 416,667 Class B non-voting shares at an exercise price of \$6.00 per Class B non-voting share. Axxent Inc. has agreed to issue additional CTRA Warrants to purchase up to 250,000 Class B non-voting shares with an exercise price of \$6.00 if certain monthly revenue thresholds are achieved over the 12-month period that began on June 17, 1999.
- In April 1999, the Company issued 17,410,000 special warrants for gross proceeds of approximately \$34.8 million. In December 1999, the special warrants were automatically exercised, for no additional consideration, for an aggregate of 5,803,333 Class A voting shares. The Company qualified the distribution of the Class A voting shares issuable upon exercise of the special warrants under a prospectus dated December 9, 1999.
- The Company granted stock options to purchase 3,024,600 Class B non-voting shares at exercise prices ranging from \$1.50 to \$16.00 per Class B non-voting share to directors, officers and key contributors pursuant to its share option plan.

PRICE RANGE AND TRADING VOLUME OF CLASS B NON-VOTING SHARES

The TSE has conditionally approved the listing of the Class B non-voting shares issuable upon exercise of the Special Warrants and the Pathway Special Warrants and upon conversion of the Series 3 preferred shares. The Class B non-voting shares commenced trading on the TSE on November 4, 1999.

The following table sets forth the reported high and low closing prices and trading volume of the Class B non-voting shares on the TSE for the periods indicated:

	<u>Period</u>	<u>High</u>	<u>Low</u>	<u>Volume</u>
2000	June (to June 9)	\$ 12.40	\$ 10.25	1,237,966
	May	15.50	10.60	2,777,300
	April	21.00	15.00	2,121,233
	March	26.50	17.60	3,740,875
	February	18.00	13.50	825,402
	January	15.05	13.25	1,128,362
1999	December	16.50	15.00	1,998,043
	November 4 - 30	17.90	12.55	5,580,690

ESCROW ARRANGEMENTS

In connection with its initial public offering, the Company was granted regulatory relief from the securities regulatory authority in the Province of Quebec in order to exempt the directors, officers and certain shareholders of the Company from applicable escrow requirements. In addition, Axxent Inc. was not required to comply with the escrow requirements of the Ontario Securities Commission since the gross proceeds of the initial public offering exceeded \$75.0 million. Accordingly, none of the Company's securities are subject to any escrow requirements imposed by the securities regulatory authority in the Province of Quebec or the Ontario Securities Commission.

CONSOLIDATED CAPITALIZATION

The following table sets forth Axxent Inc.'s capitalization as of September 30, 1999 and April 30, 2000 (i) on a historical basis, and (ii) on a pro forma basis to give effect to the automatic exercise of the Special Warrants and the Pathway Special Warrants and the issuance and conversion of the Series 3 preferred shares. This table should be read in conjunction with "Use of Proceeds", "Selected Financial Data", "Management's Discussion and Analysis of Financial Condition and Results of Operations" and the consolidated financial statements and related notes thereto included elsewhere in this prospectus.

	<u>September 30, 1999</u>		<u>April 30, 2000</u>	
	<u>Actual</u>	<u>Pro Forma Offering⁽¹⁾</u> (unaudited) (dollars in thousands)	<u>Actual</u>	<u>Pro Forma after given effect to the Offering⁽¹⁾</u>
Cash and cash equivalents.....	<u>\$ 21,392</u>	<u>\$ 306,066</u>	<u>\$ 201,586</u>	<u>\$ 201,661</u>
Long-term debt:				
15% Senior Notes Payable due 2004.....	\$ 61,480	\$ 61,480	\$ 66,250	\$ 66,250
Capital lease obligations.....	290	290	365	365
Shareholders' Equity (Deficiency):				
Class A voting shares ⁽²⁾	4,958	11,994	11,994	11,994
Class B non-voting shares ⁽²⁾⁽³⁾⁽⁵⁾⁽⁶⁾	40	313,011	147,260	317,908
Series 1 Preferred ⁽²⁾	1,250	—	—	—
Series 2 Preferred ⁽²⁾	1,250	—	—	—
Series 3 Preferred ⁽⁴⁾	—	75	—	75
Warrants ⁽⁷⁾	33,833	925	171,620	972
Deficit.....	<u>(51,064)</u>	<u>(51,064)</u>	<u>(86,872)</u>	<u>(86,872)</u>
Total shareholders' equity (deficit).....	<u>\$ (9,733)</u>	<u>\$ 274,941</u>	<u>\$ 244,002</u>	<u>\$ 244,077</u>

- (1) Includes the exercise of the Special Warrants into 10,000,000 Class B non-voting shares as well as the issuance of 33,333 Class B non-voting shares upon the exercise of the Pathway Special Warrants.
- (2) Reflects the issuance of 5,928,333 Class A voting shares and 1,180,347 Class B non-voting shares upon the automatic exercise of 17,410,000 previously issued special warrants, the automatic exercise of the Rhythms Special Warrant and the automatic conversion of an aggregate of 2,500,000 previously issued Series 1 preferred shares and Series 2 preferred shares pursuant to a prospectus dated December 9, 1999.
- (3) On October 27, 1999 Rhythms NetConnections purchased the Rhythms Special Warrant for U.S. \$5.3 million (net proceeds of approximately \$7.7 million). The Rhythms Special Warrant was exercised, for no additional consideration, for 763,680 Class B non-voting shares.
- (4) Assumes the issue and distribution of 2,448,417 Series 3 preferred shares for proceeds of \$74,653. The Series 3 preferred shares are convertible into Class B non-voting shares on a one-for-one basis.
- (5) Reflects the Company's initial public offering of 8,400,000 Class B non-voting shares on October 28, 1999 for gross proceeds of \$100,400,000. In December 1999, an over allotment option was exercised pursuant to which the Company issued an additional 1,260,000 Class B non-voting shares for additional proceeds of \$15,100,000. Total net proceeds from these offerings amounted to \$106,408,425.
- (6) Reflects the conversion of 8,281,636 Class A voting shares into Class B non-voting shares valued at approximately \$25.7 million.
- (7) Reflects the issuance, on March 28, 2000 of the Special Warrants for gross proceeds of \$180.0 million. The Special Warrants are exercisable, for no additional consideration, for 10,000,000 Class B non-voting shares.

USE OF PROCEEDS

The net cash proceeds to the Company from the issue and sale of the Special Warrants was \$170,448,351 after deducting the Underwriters' fees and the estimated expenses of the offering. The Company has or intends to use the net proceeds to finance the planned deployment of its network in its target markets and to fund the continued development of its planned services, operating losses, working capital and interest expenses.

The Company's capital plan for the period from April 1, 2000 to March 31, 2001 calls for the deployment of a voice and data network with 160 co-location sites, two main switches and 12 smaller switches in secondary markets in Ontario, Quebec, Alberta and British Columbia. This plan will require Axxent Inc. to spend approximately \$124 million

through March 31, 2001 to fund capital expenditures, the development of the Company's planned services, fund operating losses, working capital and certain interest expenses. In addition to the proceeds from the issuance and sale of the Special Warrants the Company intends to use its existing cash, the proceeds of its initial public offering and proposed vendor financing to complete this capital plan. See "Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources".

PRIVATE PLACEMENT AND PLAN OF DISTRIBUTION

On March 28, 2000, pursuant to an Underwriting Agreement, the Company issued a total of 10,000,000 Special Warrants. The Special Warrants were issued to certain purchasers on a private placement basis under applicable securities legislation. An aggregate commission of \$9,000,000 or \$0.90 per Special Warrant was paid to the Underwriters in connection with the sale of the Special Warrants. The Class B non-voting shares issuable upon exercise of the Special Warrants will be qualified for distribution under this prospectus.

The Special Warrants were issued under and are governed by a special warrant indenture dated March 28, 2000 between the Company and CIBC Mellon, as special warrant agent. The Special Warrants are exercisable until, and will be deemed to be exercised without any further act on the part of the holder, on the day (the "Expiry Date") which is the earlier of: (i) the sixth business days after a receipt is issued in the province in which the holder of Special Warrants resides for the (final) prospectus ("Final Prospectus") qualifying the issuance of the Class B non-voting shares to be issued upon exercise of the Special Warrants; and (ii) 4:59 (Toronto time) on March 28, 2001. The special warrant indenture provides that Special Warrants which have not been exercised on or before 5:00 p.m. (Toronto time) on the Expiry Date shall be automatically exercised by CIBC Mellon on behalf of the holder at that time.

Each Special Warrant entitles the holder thereof to receive, without payment of additional consideration, one Class B non-voting share. In the event that the Company has not received a receipt for the Final Prospectus from the securities regulatory authorities in each province in Canada where a holder of Special Warrants resides by July 31, 2000, each Special Warrant exercised after such date will entitle the holder thereof to 1.03 Class B non-voting shares without payment of additional consideration.

The offering price of the Special Warrants was determined by negotiation between the Company and the Underwriters.

Pursuant to the terms of the May 2000 consent solicitation, the Company agreed to issue the Series 3 preferred shares in exchange for the Note Warrants. No commission is payable in connection with the proposed issuance of the Series 3 preferred shares. Each Series 3 preferred share will be convertible for one Class B non-voting share upon payment of \$0.03 per share. The Company has agreed to use its commercially reasonable best efforts to qualify the Class B non-voting shares issuable upon conversion of the Series 3 preferred shares on or before June 30, 2000.

Pursuant to the terms of the Pathway acquisition agreement, the Company agreed to issue the Pathway Special Warrants. Each Pathway Special Warrant is exercisable, for no additional consideration, for one Class B non-voting share. The Company has agreed to use its commercially reasonable best efforts to qualify the distribution of the Class B non-voting shares issuable upon exercise of the Pathway Special Warrants.

RISK FACTORS

In evaluating the Company and its business, prospective investors should consider carefully the following risk factors in addition to other information contained in this prospectus:

Limited Operating History. Axxent Inc. commenced material operations as a reseller in January 1995, and has only recently begun to provide switch-based services out of its head office in Toronto. All the Company's revenues to date have come from the resale of local and long distance services. The Company has only recently started deploying its own network and has only recently become a CLEC. As such, the Company has only a limited operating history as a reseller, and virtually no operating history as a CLEC, upon which you can evaluate its business. The limited amount of

information about Axxent Inc. makes it more difficult for you to predict whether or not the Company will be successful. Accordingly, you will have limited historical financial information upon which to base your evaluation of the business of the Company and an investment in the Class B non-voting shares. You should consider the Company's prospects for financial and operational success in light of the risks, expenses and difficulties frequently encountered by companies in their early stage of development. See "Business of the Company".

Negative Cash Flows and Losses. For the six months ended March 31, 2000 the Company incurred operating losses of approximately \$31.1 million, net losses of approximately \$29.1 million and negative cash flow from operating and investing activities of approximately \$97.3 million. The Company's expenses have increased significantly due to rapid growth and the on-going transition of the Company to a facilities-based carrier. The Company expects its expenses and capital expenditures to continue to increase as it expands, develops and deploys its network and implements its business plan. Accordingly, the Company expects to incur significant operating losses, net losses and negative cash flow during the next several years. The Company cannot assure you that it will achieve and sustain profitability or positive net cash flow. Axxent Inc.'s inability to achieve profitability or positive cash flow in the future may have a material adverse effect on its business, financial condition and results of operations. See "Management's Discussion and Analysis of Financial Conditions and Results of Operations" and "Financial Statements".

Substantial Level of Indebtedness. At March 31, 2000, Axxent Inc. had approximately \$65.4 million of indebtedness outstanding. The Company anticipates that it may incur additional indebtedness, possibly in the near term, to finance its business plan.

This substantial level of indebtedness could have important consequences to prospective investors. For example, it could:

- limit the ability of the Company to obtain additional financing in the future for working capital, capital expenditures, debt service requirements or other purposes;
- require the Company to dedicate a substantial portion of its cash flow from operations to make payments on its indebtedness, thereby reducing the funds available to Axxent Inc. for other purposes, including working capital and capital expenditures;
- limit the flexibility of the Company in planning for, or reacting to changes in, the business of the Company or the industry in which it operates; or
- place Axxent Inc. at a competitive disadvantage compared to less leveraged competitors.

These could have a material adverse effect on the Company's business, financial condition and results of operations. See "Management's Discussion and Analysis of Financial Conditions and Results of Operations – Liquidity and Capital Resources".

Ability to Obtain Additional Capital. Deployment of the Company's operations, facilities, network and services will require significant capital expenditures. The business plan of the Company for the period from April 1, 2000 through the end of 2002 calls for the deployment of its network in the major metropolitan centres of Canada. This plan will require the Company to spend a significant amount to fund items which include the following:

- capital expenditures;
- operating losses;
- certain interest expense; and
- the deployment of its network.

The Company intends to use the net proceeds of its initial public offering and the sale of the Special Warrants to fund a portion of these needs. Axxent Inc. will still require additional financing to fund these needs as envisioned by its business plan.

Anticipated future capital expenditures of the Company are based on current estimates. Because the cost of deploying the Company's network and operating the business of the Company, as well as the ability of the Company to generate revenue, will depend on a variety of factors, actual costs and revenue may vary materially from expected amounts and such variations will affect the Company's future capital requirements.

In order to fund its business plan, Axxent Inc. may seek to obtain a working capital line of credit. The Company does not currently have a working capital line of credit and it may not be able to obtain such a line on terms acceptable to it, if at all. The lack of a working capital line of credit may impair the ability of the Company to satisfy, or respond to changes in, its cash requirements.

If the cost of deployment of the Company's planned network exceeds its current estimates or if there is a significant increase in customer demand for the Company's services in its target markets, it will have increased funding needs, possibly to a significant degree. In addition, Axxent Inc. will continue to evaluate additional revenue opportunities and strategic initiatives in each of its target markets. As attractive opportunities develop, the Company may make additional capital investments in its network or make strategic alliances or acquisitions. The Company expects that it will meet such additional funding needs by raising additional equity and/or debt capital, entering into joint ventures with strategic partners, borrowing under future credit facilities or a combination of such options. In addition, the Company continues to evaluate and seek attractive opportunities to raise additional equity capital in anticipation of future capital requirements. The Company can provide no assurance, however, that the terms of the 1997 Notes or any other credit facility will permit Axxent Inc. to raise sufficient additional debt capital. The Company may be limited in its ability to raise additional equity capital outside of Canada due to Canadian legal restrictions that limit the extent of non-Canadian ownership and control of Canadian telecommunications carriers and their holding companies. See "Regulation". The Company can provide no assurance that it will be successful in raising sufficient additional debt or equity capital, or that such options, if available at all, will be available on a timely basis or on terms acceptable to it. Failure to raise sufficient funds may require Axxent Inc. to delay or abandon some of its planned future expansion or expenditures, which could have a material adverse effect on the Company's business, financial condition and results of operations and could cause the business of the Company to suffer or even fail.

Variability of Operating Results. As a result of the timing of the significant expenses associated with the deployment the Company's network, it is anticipated that the operating results of the Company could vary significantly from period to period. Such variability could have a material adverse effect on the Company's business, financial condition and results of operations.

Successful Implementation of the Business Plan. If the Company fails to execute its strategy in a timely or effective manner, it may be unable to compete successfully in its target markets. The business strategy of the Company is complex and requires Axxent Inc. to achieve many objectives. In order to implement the business plan, the Company must:

- design, deploy, operate and maintain its network;
- maintain support systems such as the billing system and customer care systems;
- migrate existing customers from resale of local loops and long distance service to the Company's switch-based network service;
- attract and retain customers and skilled employees;
- expand its sales presence in existing and new markets;
- acquire and integrate existing businesses that contribute to the growth strategy of the Company; and

- develop and provide enhanced services.

If the Company is unable to achieve these objectives, the Company's business is likely to suffer or even fail. See "Business – Business Strategy".

Limited Experience. The Company is currently offering local carrier services to its customers primarily by reselling services acquired from the ILECs. At this time Axxent Inc. is only providing limited switch-based services to customers in Toronto and Montreal. The Company is still deploying the initial phase of its network and has limited experience designing, deploying and operating a telecommunications network. See "Business of the Company". The Company cannot assure you that it will effectively design, deploy and operate the network, or that the network will function as planned. The Company may not be able to deploy its network within the time frame expected, and once the network is deployed the Company may encounter unanticipated difficulties in operating and maintaining it. If the Company is unable to implement its switch-based strategy design, deploy and operate its network effectively, or if the network does not function as planned the Company's business is likely to suffer or even fail.

Rapid Technological Changes. The telecommunications industry is subject to rapid and significant changes in technology. The Company cannot predict the effect that changes in technology will have on the Company's business or whether such changes will require Axxent Inc. to expend more resources to develop its network than are currently expected. Any such changes could have a material adverse effect on the Company's business, operating results and financial condition. See "Industry Background" and "Business of the Company – Competition".

Increases in Customer Attrition Rates. The Company cannot assure you that its customers will continue to purchase local, long distance or other services from it or purchase additional services from it or that customers will migrate to its network in accordance with its business plan. Axxent Inc. could lose customers as a result of national advertising campaigns, telemarketing programs, customer incentives or new technologies provided by major competitors as well as for other reasons outside of the control of the Company. Increases in the Company's customer attrition rates could have a material adverse effect on the Company's business, results of operations and financial condition.

Migration of Customers. The Company cannot assure you that it will be able to migrate its customers from the ILECs to its own network switches in accordance with its business plan. Customers could object to being migrated to the Company's network and may encounter technical difficulties in doing so. A failure to migrate customers to the Company's own switches could have a material adverse effect on the Company's business, results of operations and financial condition. See "Business of the Company – Migration of Current Customers".

Failure of the Company's Information Systems. The accurate and prompt billing of customers is essential to the operations and future profitability of the Company. The Company's billing and collection activities are dependent upon it gathering, as well as Axxent Inc.'s principal suppliers providing it with, accurate call data records. If the Company does not receive accurate call data records in a timely manner, the Company's business, financial condition and results of operations could be materially adversely affected. Moreover, the deployment of the Company's network will place significant demands on its billing and management systems. The Company cannot assure you that its billing and management systems will be sufficient to provide it with accurate and efficient billing and other necessary processing capabilities. The Company may not identify all of its information and processing needs and may not be able to upgrade its information systems as needed. Either of these could have a material adverse effect on the Company's business, financial condition and results of operations.

The Company has developed a new information system to integrate important facets of its operations. The implementation of this system relies in part on the products and services of third party vendors, over which the Company has no control. Furthermore, such products and services must be successfully integrated. The failure of the Company to accomplish the transition to this new system, or unanticipated problems with the new system, could have a material adverse effect on the Company's business, financial condition and results of operations. See "Business of the Company – Network" and "Business of the Company – Information Systems".

Reliability of the Networks, Services and Equipment of Third Party Providers. The Company only provides limited services over its network, which is currently operating only in one area of Toronto and Montreal. At present,

Axxent Inc. depends almost entirely on switch-based carriers, including ILECs, for switching and transmission of customer traffic. After the deployment of the Company's network is completed, the Company will still rely on others for fibre optic transmission facilities for the network. The Company cannot be sure that any third party switching or transmission facilities will be available to it when needed or on acceptable terms.

Although the Company can exercise direct control over the customer care and support it provides, most of the services currently offered by the Company are provided by others. These services are subject to physical damage, power loss, capacity limitations, software defects, breaches of security and other factors which may cause interruptions in service or reduced capacity for the Company's customers. These problems, although not within the control of the Company, could adversely affect customer confidence and damage Axxent Inc.'s reputation. In addition, the Company has an agreement with Nortel to purchase switches and related electronic equipment to facilitate the implementation of the Company's business plan, but will require additional supply arrangements. If the Company fails to enter into any other required supply arrangements, or if there are any reductions or interruptions in supply or material increases in the price of equipment or services to be purchased from Nortel or other suppliers, the Company may suffer disruptions in the development and expansion of its network or the operation of its business, or incur higher than expected capital costs. Such increased costs could have a material adverse effect on the Company's business, financial condition and results of operations.

Dependence on the ILECs. The Company provides local services to certain customers utilizing facilities and services leased or purchased from the ILECs. The ILECs are the principal competitors of the Company and currently dominate the local services market. While the ILECs currently are not entitled to discriminate against carriers such as Axxent Inc. in the rates or services they provide, or in respect of access to their facilities, the Company is vulnerable to changes in lease and interconnection arrangements with the ILECs and changes in CRTC policy. ILECs are not limited in the markup they may charge CLECs for certain non-essential services and, as a result, are able to compete against CLECs using such non-essential services on the basis of price alone, if they so choose. The ability of the Company to provide enhanced connectivity to its network and to provide local dial tone services will require it to negotiate or renew interconnection agreements with ILECs. This can take considerable time, effort and expense, and these agreements are subject to Canadian federal regulation. The Company may not be able to effectively negotiate necessary interconnection agreements on acceptable terms or at all. See "Regulation".

Year 2000 Compliance. The Year 2000 problem arose from the fact that many computer programs indicated the year by only two digits, rather than four. As a result, it was generally thought that computer systems and software in a wide variety of industries would possibly produce some erroneous results unless they were modified or upgraded to process data information correctly. Although the change in date has occurred, it is not possible to conclude that all aspects of the Year 2000 problem that may affect the Company have been fully resolved. Despite the fact that many computer systems are currently processing 21st century dates correctly, the Company could experience latent Year 2000 problems. If the Company is unable to address any latent Year 2000 compliance issues, or if third party vendors, licensors and providers of hardware, software and services with which the Company conducts business do not successfully address these issues, the Company could experience service interruptions, unexpected expenses and delays, including delays in its ability to conduct normal business operations and sell its products and services, and a loss of customers. As of the date of this Prospectus, the Company has not experienced any Year 2000 interruptions or other issues relating to its network equipment, software, computer technology or services.

Availability and Condition of Telephone Lines. The Company's ability to provide DSL-based services to its customers depends on the quality, physical condition, availability and maintenance of telephone lines within the control of the ILECs. Management believes that the current condition of telephone lines in some cases may be inadequate to permit Axxent Inc. to fully implement such services. In addition, the ILECs may not continue to maintain the telephone lines in a condition that will allow Axxent Inc. to support effective application of such services in the longer term. The ILECs may, at some point, claim that their facilities are not of sufficient quality to allow the Company to fully implement or operate its DSL-based services despite the fact that such a claim may well encumber their own initiatives involving similar DSL technology. Further, ILEC service to some areas may use technologies other than local loops and, in such cases, DSL technology may not be an available option for the Company in providing service. An inability to rely on DSL technology in providing its current and planned services could have a material adverse effect on the Company's business, results of operations and financial condition.

Interference or Claims of Interference. All transport technologies deployed on copper telephone lines have the potential to interfere with, or to be interfered with by, other transport technologies on the copper telephone lines. Management believes that DSL technologies, like other transport technologies, do not interfere with existing voice services and that a workable plan that takes into account all technologies could be implemented in a scalable way across the ILECs using existing plant engineering principles. Management believes there are several initiatives underway to establish national standards and principles for the deployment of DSL technologies which, among other things, are directed at controlling such interference within acceptable limits and that the Company's DSL technologies can be deployed consistently with these evolving standards. Nevertheless, the ILECs may claim that the potential for interference permits them to restrict or delay the Company's deployment of DSL services despite the fact that this could also compromise their own deployment of similar services. Interference could degrade the performance of Axxent Inc. services or make the Company unable to provide such services on selected lines. The procedures to resolve interference issues between competitive carriers and the ILECs are still being developed, and these procedures may not be effective. The Company may be unable to successfully negotiate interference resolution procedures with the ILECs. Moreover, the ILECs may make claims regarding interference or unilaterally take action to resolve interference issues to the detriment of the Company's services. The CRTC could also institute responsive actions in response to interference claims favouring the ILECs rather than new competitors. Interference, or claims of interference, if widespread, could have a material adverse effect on the speed of deployment of the Company's network, and on the reputation, brand image, service quality and customer satisfaction and retention of the Company as a whole.

No Voting Rights. The Class B non-voting shares have no voting rights, except as required by law. Holders of the Class B non-voting shares have no right to vote in the election of directors or to vote on most matters requiring shareholder approval. See "Description of Share Capital".

Influence in respect of any Matter Requiring Shareholder Approval. The executive officers, directors, and principal shareholders of the Company control approximately 79.5% of the outstanding Class A voting shares after giving effect to the exercise of the Special Warrants. This concentration of ownership may delay, deter or prevent actions that would otherwise result in a change of control and could have a material adverse effect on the market price of the Class B non-voting shares. See "Principal Shareholders" and "Description of Capital Stock".

Restrictions on Foreign Ownership. Under the *Telecommunications Act*, the Company's operating subsidiary is not eligible to operate as a Canadian carrier to provide local switched services in Canada unless it is Canadian-owned and controlled. To qualify as a Canadian-owned carrier, no more than 20% of the members of the Company's board of directors may be non-Canadians, and no more than 20% of the voting shares of the Company may be beneficially owned by non-Canadians. In addition, because Axxent Inc. is a non-operating parent corporation holding a Canadian carrier, no more than 33 $\frac{1}{3}$ % of the voting shares of Axxent Inc. may be beneficially owned by non-Canadians. These Canadian ownership restrictions may limit the ability of the Company to raise equity capital outside of Canada in the future. Although management believes that the Company is in compliance with the relevant legislation, there can be no assurance that a future CRTC determination or events beyond the Company's control will not result in Axxent Inc. ceasing to comply with the relevant legislation. Should this occur, the ability of the operating subsidiary to operate as a Canadian carrier under the *Telecommunications Act* could be jeopardized and the business of the Company could be materially adversely affected. If the Company becomes subject to proceedings with respect to compliance with the relevant legislation, it could be materially adversely affected, even if Axxent Inc. is ultimately successful in such a proceeding. See "Regulation".

Immediate Dilution. The effective price of each Class B non-voting share issuable or deliverable upon the exercise or conversion of the Special Warrants, the Pathway Special Warrants and the Series 3 preferred shares will be substantially higher than the net tangible book value per share of the outstanding Class B non-voting shares. As a result, the Class B non-voting shares will be subject to immediate and substantial dilution. In addition, the Company has issued options to acquire Class B non-voting shares at prices significantly below the effective price of each Class B non-voting share. The Class B non-voting shares may be subject to additional dilution if holders of stock options, whether currently outstanding or subsequently granted, exercise their options. See "Dilution".

The Market Price of the Class B Non-Voting Shares Could be Volatile. The trading price of the Class B non-voting shares could be subject to wide fluctuations in response to certain factors affecting the Company and its competitors. In addition, in recent years the stock market has experienced extreme price and volume fluctuations. These fluctuations have had a substantial effect on the market prices for many emerging growth companies, often unrelated to the operating performance of the specific companies. Such market fluctuations could have a material adverse effect on the market price of the Class B non-voting shares.

Significant Government Regulation. The Company's network and the provision of switched and private line services are subject to significant government and industry regulation. The telecommunications industry in general, and the market for local switched services in particular, are undergoing substantial regulatory change and uncertainty. Future regulatory, judicial or legislative changes, or other regulatory activities, could have a material adverse effect on the Company's business, financial condition and results of operations. See "Regulation".

Changes in the Value of the Canadian Dollar. For the purposes of financial reporting, any change in the value of the Canadian dollar against the U.S. dollar during a given financial reporting period would result in a foreign exchange loss or gain on the translation of any U.S. cash and cash equivalents and a deferred loss or gain on the translation of U.S. dollar-denominated long term monetary items into Canadian currency. Therefore, the reported earnings of the Company could fluctuate materially as a result of foreign exchange translation losses or gains and amortization of deferred losses or gains. Changes in the currency exchange rate could have a material adverse effect on the Company and its ability to make payments on U.S. dollar-denominated debt. See "Description of Certain Indebtedness".

Requirement for Dividends to Meet Cash Requirements. Axxent Inc. is a holding company with no business operations of its own. The only significant asset of Axxent Inc. is the outstanding shares of its operating subsidiary. Accordingly, its only source of cash to pay interest and principal on outstanding indebtedness is through distributions relating to its ownership interest in its subsidiary from net earnings and cash flow generated by its subsidiary. The Company expects that the earnings and cash flow of its subsidiary will be retained and used by them in its operations, including to service its debt obligations. See "Dividend Policy".

Terms of Indebtedness. The terms of the Company's current debt instruments contain, and future debt instruments may contain, a number of significant covenants. Any of such limitations could have a material adverse effect on the Company's business, financial condition and results of operations. In addition, if the Company fails to comply with any of the covenants, its debt may be accelerated by the holders of such debt, and the business of the Company could suffer or even fail. See "Description of Certain Indebtedness".

Absence of Cash Dividends. The Company does not intend to pay cash dividends on its Class A voting shares or Class B non-voting shares for the foreseeable future. The Company currently intends to retain earnings for reinvestment in the business and repayment of indebtedness. In addition, the terms of certain existing debt instruments contain, and future debt instruments may contain, restrictions on the ability of the Company to pay dividends or to make distributions. The Company currently does not anticipate making distributions in respect of its share capital. However, if such determination were made, there can be no assurance that the Company's subsidiaries will generate sufficient cash flow to pay or distribute such a dividend. See "Dividend Policy" and "Description of Certain Indebtedness".

Dependence on Personnel. Management believes that the success of the Company depends upon the abilities and continued efforts of its management, particularly members of the senior management team, including the sales and marketing consultants. The loss of the services of any of these individuals could have a material adverse effect on the Company's business, results of operations and financial condition. The success of the Company will also depend upon its ability to identify, hire and retain additional highly skilled management, sales, and marketing, service and technical personnel. Demand for skilled personnel with telecommunications experience is high and competition for their services is intense. The Company has recently hired a new President and Chief Executive Officer. Axxent Inc. cannot assure you that this new senior officer will be effective in managing the Company or will successfully work with the existing management team. The Company expects the former Chief Executive Officer to continue to serve in a senior executive position after the employment of this new executive, but cannot assure you that he will do so or effect an orderly transition to the new executive. The failure to retain the services of the former Chief Executive Officer could have a

material adverse effect on the Company's business, financial condition and results of operations. See "Management – Directors, Executive Officers and Key Consultants".

Highly Competitive Industry. The Company operates in a highly competitive environment. Axxent Inc. has no significant market share in any market in which it operates and faces intense competition in all of its markets for its existing and planned services from the ILECs, cable companies, long distance providers, data carriers, wireless providers, new CLEC entrants, and Centrex and other resellers. Most of the Company's current and potential competitors have a longer operating history in the telecommunications industry and financial, marketing, technical, personnel, regulatory and other resources that are substantially greater than Axxent Inc.. Management believes that the CRTC's Local Competition Decision will accelerate competition for all types of local switched services which the ILECs currently dominate and expect competition to intensify as competitors attempt to gain a share of markets experiencing limited growth. In each of the markets the Company proposes to serve, Axxent Inc.'s principal competitor will be the ILEC serving that geographic area or, potentially, another ILEC seeking to compete in that geographic area. The ILECs have long-standing relationships with their customers and, until recently, have benefited from a monopoly over the provision of local switched services. In addition, the ILECs have resources that exceed those of the Company. Axxent Inc. may not be able to successfully offer services in competition with the ILECs. See "Business of the Company – Competition".

Successful Completion and Integration of Acquisitions. The Company has recently completed several significant acquisitions. An element of the Company's business strategy is to acquire companies and take advantage of other growth opportunities that will complement and expand its operations on acceptable terms. Competition for attractive companies in the telecommunications industry is substantial. The Company may not be able to identify or complete future acquisitions or realize the anticipated results of future acquisitions. Acquisitions may involve numerous risks, including difficulty in integrating operations, technologies, systems, and products and services of acquired companies, diversions of management's attention and disruption of operations, increased expenses and working capital requirements, entering markets in which competitors have stronger market positions and the potential loss of key employees and customers of acquired companies. In addition, acquisitions may involve financial risks, such as the potential liabilities of the acquired businesses, the dilutive effect of the issuance of additional equity securities, the incurrence of additional debt, the financial impact of transaction expenses and the amortization of goodwill and other intangible assets involved in any transactions that are accounted for using the purchase method of accounting, and possible adverse tax and accounting effects. If realized, any of these risks could have a material adverse effect on the Company's business, results of operations and financial condition.

Forward Looking Statements. Certain statements about the Company and the telecommunications industry under the captions "Summary", "Risk Factors", "Use of Proceeds", "Description of Certain Indebtedness", "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Business of the Company" and elsewhere in this prospectus are forward-looking statements. These forward-looking statements include, but are not limited to, statements about the Company's plans, objectives, expectations, intentions and assumptions and other statements in this prospectus that are not historical facts. When used in this prospectus, the words "estimate", "project", "believe", "anticipate", "intend", "plan", "expect" and similar expressions are generally intended to identify forward-looking statements. Because these forward looking statements involve risks and uncertainties, including those described in this "Risk Factors" section, actual results could differ materially from those expressed or implied by these forward-looking statements. The Company cautions you not to place undue reliance on these forward-looking statements. These forward-looking statements speak only as of the date of this prospectus. The Company does not undertake any obligation to publicly release any revisions to these forward-looking statements to reflect new information, future events or otherwise.

DILUTION

The following table sets out the amount by which the price per Class B non-voting share exceeds the consolidated net tangible book value of the Class A voting and Class B non-voting shares as at April 30, 2000 after giving effect to the issue and distribution of the Class B non-voting shares to be issued upon exercise or conversion, as the case may be, of the Special Warrants, the Pathway Special Warrants and the Series 3 preferred shares:

	<u>Per Share</u>
Offering Price	\$ 18.00
Net tangible Book Value before the Offering	\$ 1.82
Increase in Net Tangible Book Value attributable to the Offering	<u>\$ 3.80</u>
Pro forma Net Tangible Book Value after the Offering	\$ 5.62
Dilution to Subscribers	<u>\$ 12.38</u>
Dilution as a Percentage of the Offering Price	69%

DIVIDEND POLICY

To date, the Company has not paid any dividends to its shareholders. The Company intends to retain its earnings and does not currently expect to pay cash dividends.

MATERIAL CONTRACTS

Except for agreements entered into in the ordinary course of business, the only material agreements or other contractual arrangements entered into by or on behalf of the Company within the two years preceding the date of this prospectus are as follows:

- (a) the Underwriting Agreement described under “Private Placement and Plan of Distribution”;
- (b) Special Warrant indenture described under “Private Placement and Plan of Distribution”;
- (c) the securities purchase agreement dated December 31, 1997 between the Company and the purchasers of the 1997 Notes;
- (d) the warrant agreement dated December 31, 1997 between the Company and the holders of the Note Warrants of the Company;
- (e) the April 1999 consent solicitation between the Company and the holders of the Note Warrants of the Company;
- (f) the December 1999 consent solicitation between the Company and the holders of the Note Warrants of the Company;
- (g) the May 2000 consent solicitation between the Company and the holders of the Note Warrants of the Company; and
- (h) the Rhythms Joint Venture Agreement described under “Business of the Company – Rhythms Canada Joint Venture”.

Copies of these agreements, or the relevant provisions thereof, will be available for inspection by the holders of Special Warrants at the head office of the Company during normal business hours until 30 days following the date on which a final receipt is issued for this prospectus.

LEGAL MATTERS

Certain legal matters relating to the issuance of the Special Warrants and the distribution of the Class B non-voting shares upon the exercise or deemed exercise of the Special Warrants will be passed upon on behalf of the Company by Wildeboer Rand Thomson Apps & Dellelce, LLP, and on behalf of the Underwriters by Blake, Cassels & Graydon LLP. Perry Dellelce, a partner of Wildeboer Rand Thomson Apps & Dellelce, LLP is a director of the Company.

AUDITORS, REGISTRAR AND TRANSFER AGENT

The auditors of the Company are Deloitte & Touche LLP, Chartered Accountants, 181 Bay Street, Suite 1400, Toronto, Ontario M5J 2V1.

The registrar and transfer agent for the Class B non-voting shares is CIBC Mellon Trust Company of Canada at its principal offices in Toronto, Ontario.

The special warrant agent for the Special Warrants is CIBC Mellon Trust Company of Canada at its principal offices in Toronto, Ontario.

PURCHASERS' STATUTORY RIGHTS

Securities legislation in certain of the provinces of Canada provides purchasers with the right to withdraw from an agreement to purchase securities within two business days after receipt or deemed receipt of a prospectus and any amendment. In several of the provinces, applicable securities legislation further provides a purchaser with remedies for rescission or, in some jurisdictions, damages where the prospectus and any amendment thereto contains a misrepresentation or is not delivered to the purchaser, provided that such remedies for rescission or damages are exercised by the purchaser within the time limit prescribed by the securities legislation of such province. A purchaser should refer to any applicable provisions of the securities legislation of his or her province for the particulars of these rights or consult with a legal adviser.

CONTRACTUAL RIGHT OF ACTION FOR RESCISSION

In the event that a holder of Special Warrants that acquires Class B non-voting shares upon the exercise of the Special Warrants as provided for in this prospectus, is or becomes entitled under applicable securities legislation to the remedy of rescission by reason of this prospectus or any amendment hereto containing a misrepresentation, any such holder shall be entitled to rescission not only of the holder's exercise of its Special Warrants but also of the private placement transaction pursuant to which the Special Warrants were initially acquired, and shall be entitled in connection with such rescission to a full refund of all consideration paid on the acquisition of the Special Warrants. In the event such holder is a permitted assignee of the interest of the original Special Warrant subscriber, such permitted assignee shall be entitled to exercise the rights of rescission and refund granted hereunder as if such permitted assignee was such original subscriber. The foregoing rights are in addition to any other right or remedy available to a holder of Special Warrants under section 130 of the *Securities Act* (Ontario) or otherwise at law.

Consolidated Financial Statements of

AXXENT INC.
(formerly “OCI Communications Inc.”)

September 30, 1999, 1998 and 1997
and
(unaudited) March 31, 2000 and 1999

Auditors' Report

To the Directors of
AXXENT Inc.
(formerly "OCI Communications Inc.")

We have audited the consolidated balance sheets of Axxent Inc. (formerly "OCI Communications Inc.") as at September 30, 1999 and 1998 and the consolidated statements of operations and deficit and cash flows for the years ended September 30, 1999, 1998 and 1997. 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 audits.

We conducted our audits 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 our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at September 30, 1999 and 1998 and the results of its operations and its cash flows for the years ended September 30, 1999, 1998 and 1997 in accordance with Canadian generally accepted accounting principles.

Chartered Accountants

Toronto, Ontario
December 13, 1999 (except as to notes 1 and 18 which are as of May 29, 2000)

AXXENT INC. (formerly, "OCI Communications Inc.")

Consolidated Balance Sheets

	March 31,		September 30,	
	2000	1999	1999	1998
	(unaudited)	(unaudited)		
ASSETS				
CURRENT				
Cash and short-term investments	\$ 208,867,908	\$ 21,645,972	\$ 21,392,381	\$ 27,276,786
Accounts receivable	14,730,113	8,302,737	10,483,635	8,024,082
Other receivables	4,586,487	299,514	2,625,017	—
Prepaid expenses and deposits (note 3)	3,292,429	1,474,418	2,389,260	867,877
	231,476,937	31,722,641	36,890,293	36,168,745
INVESTMENT IN JOINT VENTURE (note 4)	7,250,000	—	—	—
DEFERRED ASSETS (note 5)	3,720,722	2,425,437	3,533,576	2,217,159
CAPITAL ASSETS (note 6)	71,526,956	2,720,542	28,557,345	2,306,063
GOODWILL (note 7)	25,991,957	—	7,483,996	—
	<u>\$ 339,966,572</u>	<u>\$ 36,868,620</u>	<u>\$ 76,465,210</u>	<u>\$ 40,691,967</u>
LIABILITIES				
CURRENT				
Accounts payable and accrued liabilities (note 8)	\$ 20,221,408	\$ 6,237,518	\$ 22,407,812	\$ 6,146,313
Deferred revenue and customer deposits	5,325,229	2,586,305	4,260,664	2,140,553
Capital lease obligations - current portion (note 9)	345,456	—	60,878	—
	25,892,093	8,823,823	26,729,354	8,286,866
SENIOR NOTES PAYABLE (note 10)	63,104,285	55,138,646	59,240,054	51,262,368
CAPITAL LEASE OBLIGATIONS - long term (note 9)	259,696	—	229,078	—
	89,256,074	63,962,469	86,198,486	59,549,234
SHAREHOLDERS' EQUITY (DEFICIT)				
Share capital (note 11)	159,353,265	4,960,375	7,497,775	4,957,125
Special warrants (note 11)	171,519,992	—	33,832,719	—
Deficit	(80,162,759)	(32,054,224)	(51,063,770)	(23,814,392)
	250,710,498	(27,093,849)	(9,733,276)	(18,857,267)
	<u>\$ 339,966,572</u>	<u>\$ 36,868,620</u>	<u>\$ 76,465,210</u>	<u>\$ 40,691,967</u>

Approved on Behalf of the Board

(signed) Perry Dellelce
Director

(signed) Stephen Coxford
Director

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

AXXENT INC. (formerly “OCI Communications Inc.”)
Consolidated Statement of Operations and Deficit

	Six months ended March 31,		Year ended September 30,		
	2000	1999	1999	1998	1997
	(unaudited)	(unaudited)			
REVENUES	\$ 29,851,905	\$ 21,308,177	\$ 45,860,184	\$ 31,693,882	\$ 12,974,782
COST OF SERVICES	22,503,888	15,590,838	33,901,387	23,552,573	10,014,628
GROSS PROFIT	7,348,017	5,717,339	11,958,797	8,141,309	2,960,154
EXPENSES					
Selling, general and administrative	28,321,856	9,355,400	27,224,954	14,172,647	6,701,909
Interest expense	4,669,990	3,928,195	8,395,702	6,463,784	568,714
Depreciation and amortization	5,590,205	1,163,070	3,967,479	1,873,652	653,107
Financing expenses	—	—	834,481	3,716,875	—
Foreign exchange (gain) loss	(127,145)	139,361	306,646	75,765	—
	38,454,906	14,586,026	40,729,262	26,302,723	7,923,730
OPERATING LOSS FOR THE PERIOD	(31,106,889)	(8,868,687)	(28,770,465)	(18,161,414)	(4,963,576)
OTHER INCOME					
Interest	2,007,900	628,855	1,521,087	1,263,408	—
NET LOSS FOR THE PERIOD	(29,098,989)	(8,239,832)	(27,249,378)	(16,898,006)	(4,963,576)
DEFICIT, BEGINNING OF PERIOD	(51,063,770)	(23,814,392)	(23,814,392)	(6,916,386)	(1,952,810)
DEFICIT, END OF PERIOD	\$ (80,162,759)	\$ (32,054,224)	\$ (51,063,770)	\$ (23,814,392)	\$ (6,916,386)
BASIC LOSS PER SHARE (note 13)	\$ (1.36)	\$ (0.87)	\$ (2.88)	\$ (1.79)	\$ (0.76)
WEIGHTED AVERAGE SHARES OUTSTANDING	21,380,956	9,467,142	9,471,012	9,441,556	6,543,866

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

AXXENT INC. (formerly “OCI Communications Inc.”)
Consolidated Statement of Cash Flows

	Six months ended March 31,		Year ended September 30,		
	2000	1999	1999	1998	1997
	(unaudited)	(unaudited)			
NET (OUTFLOW) INFLOW OF CASH RELATED TO THE FOLLOWING ACTIVITIES					
OPERATING					
Net loss for the period	\$(29,098,989)	\$(8,239,832)	\$(27,249,378)	\$(16,898,006)	\$(4,963,576)
Item not affecting cash					
Depreciation and amortization	5,590,205	1,163,070	3,967,479	1,873,652	653,107
	(23,508,784)	(7,076,762)	(23,281,899)	(15,024,354)	(4,310,469)
Changes in non-cash working capital items					
Accounts receivable and other receivables	(6,238,420)	(578,169)	(5,084,317)	(3,473,142)	(3,524,336)
Prepaid expenses and deposits	(863,049)	(606,541)	(1,521,636)	(429,708)	(326,806)
Accounts payable and accrued liabilities	(5,687,947)	133,340	8,303,274	1,333,677	1,604,327
Deferred revenue and customer deposits	1,064,565	445,752	1,250,715	959,070	910,535
Interest payable	3,984,397	3,834,144	10,217,447	1,927,300	-
	(31,249,238)	(3,848,236)	(10,116,416)	(14,707,157)	(5,646,749)
FINANCING					
Issuance of senior notes	-	-	-	51,262,368	-
Issuance of share capital	114,297,771	3,250	40,650	9,000	2,500,000
Issuance of special warrants	170,494,992	-	32,707,719	-	-
(Repayment of) proceeds from shareholder loans	-	-	-	(4,399,558)	4,399,558
(Repayment of) proceeds from loans payable	-	-	-	(548,434)	(1,160,148)
Payment of capital lease obligations	(29,593)	-	(54,471)	(223,275)	-
	284,763,170	3,250	32,693,898	46,100,101	5,739,410
INVESTING					
Purchase of capital assets	(44,289,868)	(720,711)	(21,086,335)	(1,667,040)	(1,122,090)
Proceeds from sale of capital assets	1,272,361	-	-	-	-
Acquisition of subsidiaries net of cash acquired	(14,899,717)	-	(4,152,978)	-	-
Acquisition of subsidiaries net assets acquired	536,576	-	70,957	-	-
Investment in joint venture	(7,250,000)	-	-	-	-
Increase in deferred assets	(1,407,757)	(1,065,117)	(3,293,531)	(2,563,257)	(980,796)
	(66,038,405)	(1,785,828)	(28,461,887)	(4,230,297)	(2,102,886)
INCREASE (DECREASE) IN CASH AND SHORT-TERM INVESTMENTS					
	187,475,527	(5,630,814)	(5,884,405)	27,162,647	(2,010,225)
CASH AND SHORT-TERM INVESTMENTS, BEGINNING OF PERIOD					
	21,392,381	27,276,786	27,276,786	114,139	2,124,364
CASH AND SHORT-TERM INVESTMENTS, END OF PERIOD					
	\$208,867,908	\$ 21,645,972	\$21,392,381	\$27,276,786	\$114,139
SUPPLEMENTARY CASH FLOW INFORMATION					
Interest Paid	86,000	-	71,000	4,526,000	580,000

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

**AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements**

1. BASIS OF PRESENTATION

These consolidated financial statements reflect the operations of Axxent Inc. (“the Company”) and its wholly owned subsidiary, Axxent Corp. (“Axxent Corp.”) (formerly, “Optel Communications Corporation”).

The Company was incorporated under the *Business Corporations Act* (Ontario) on February 2, 1999 as an Ontario numbered company to own all of the issued and outstanding shares of Axxent Corp. In April 1999, the Company completed the reorganization that gave effect to this holding company/operating company structure. By articles of amendment dated April 1, 1999, the Company changed its name to Optel Communications Inc. and created the Class A voting shares and Class B non-voting shares. By articles of amendment dated July 30, 1999, the Company created the Series 1 preferred shares and Series 2 preferred shares. By articles of amendment dated September 16, 1999, Optel Communications Inc. changed its name to OCI Communications Inc. and by articles of amendment dated May 29, 2000, changed its name to Axxent Inc.

The unaudited interim consolidated balance sheets as at March 31, 2000 and 1999 and the unaudited interim consolidated statements of operations and deficit and cash flows for the six months ended March 31, 2000 and 1999, in the opinion of management, have been prepared on the same basis as the audited consolidated financial statements and include all adjustments necessary for the fair statement of the results of the interim periods. All adjustments reflected in these interim consolidated financial statements for these periods are also unaudited. Results for the six month periods ended March 31, 2000 and 1999 are not necessarily indicative of the results to be expected for the full year.

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. Significant accounting policies are outlined below:

Revenue recognition

The Company’s revenues are derived primarily from offering local and long distance telecommunications services on a recurring basis to their customers. Revenues from these services are recognized on a monthly basis as the services are provided.

Recurring monthly service fees that are invoiced in advance of the services being provided are recorded as deferred revenue and recognized as revenue in the period in which the services are provided.

AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

Cash and short-term investments

The Company’s short-term investments have an original maturity of less than three months and, accordingly, are considered to be cash equivalents. Short-term investments are recorded at cost plus accrued interest earned, which approximates current market value.

Deferred assets

Deferred installation costs and deferred promotion costs are amortized over 2 years which corresponds to the average length of a customer contract.

Capital assets

Capital assets are recorded at cost and are depreciated on a straight line basis at annual rates based on their estimated useful lives as follows:

Telecommunications network	7-15 years
Billing system	5 years
Computer hardware and software	3 years
Furniture and fixtures	5 years
Leasehold improvements	5 years
Office equipment	5 years
Other assets	5 years
Office equipment under capital lease	5 years

Goodwill

Goodwill represents the excess of the purchase price over the fair values of net assets acquired. Goodwill is amortized on a straight-line basis over a seven-year period. The Company regularly reviews the carrying value of its goodwill to determine whether there has been a permanent impairment in value. The measurement of possible impairment is based primarily on the ability to recover the carrying value from expected future operating cash flows on an undiscounted basis.

Derivative financial instruments

The Company has entered into a foreign currency option contract to hedge the effect of exchange rate changes on foreign currency denominated debt. Any gain or loss associated with the option contract will be recorded as a component of the debt repayment transaction. The premium on the option is deferred and amortized over the life of the option.

Long term debt

The U.S. dollar denominated long term debt is hedged with the foreign currency option contract which can be exercised at any time up to the maturity date of January 2, 2001. The contract has fixed the maximum exchange rate of the debt at CAD \$1.47. As a result of this transaction, the long-term debt is also translated into Canadian dollars at the hedged rate of \$1.47. Any unrealized gain and losses resulting from the translation at the exchange rate prevailing at the time the hedge

**AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements**

2. SIGNIFICANT ACCOUNTING POLICIES (continued)

was established and the year-end rate are deferred and amortized over the remaining term of the related obligation.

Income taxes

The Company provides for income taxes based on accounting income using the deferral method. Under this method, taxes are computed using current tax rates regardless of when such income is subject to taxes under the tax laws. The deferred tax balances which result, if any, are not adjusted for any subsequent changes in tax rates.

Segmented information

The Company is a telecommunications provider of voice, data, and Internet services comprising a single operating segment. All of the Company’s assets are located in Canada and revenues are derived from services provided in Canada.

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 reporting period. Actual results could differ from those estimates.

3. PREPAID EXPENSES AND DEPOSITS

	March 31, 2000 1999 (unaudited)		September 30, 1999 1998	
Prepaid expenses	\$ 1,869,656	\$ 1,096,202	\$ 1,177,271	\$ 753,067
Cost of Initial Public Offering	—	—	878,456	—
Deposits	1,422,773	378,216	333,533	114,810
	<u>\$ 3,292,429</u>	<u>\$ 1,474,418</u>	<u>\$ 2,389,260</u>	<u>\$ 867,877</u>

4. UNAUDITED - INVESTMENT IN JOINT VENTURE

On January 1, 2000, Axxent Corp. signed a joint venture agreement with Rhythms NetConnections, Inc. (“Rhythms”) to form Rhythms Canada Inc. (“RCI”). This joint venture was established for the purpose of developing a DSL network that will offer high speed DSL data services to wholesale and enterprise customers. On February 28, 2000, Axxent Corp. subscribed for \$14,500,000 (U.S. \$10,000,000) in cash consideration of retractable, non-voting, non-convertible preference shares in the capital of RCI. Rhythms had previously purchased a special warrant of the Company for \$7,743,393 (U.S. \$5,300,000). The special warrant was exercised, for no additional consideration, for 763,680 Class B non-voting shares of the Company on December 14, 1999.

AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements

The following is a summary of the company’s 50% proportionate share of the unaudited Balance Sheet, unaudited Statements of Operations, and Cash Flows for RCI:

	March 31, 2000 (unaudited)
Balance Sheet	
Current assets	\$ 6,422,182
Non-current assets	1,438,052
Total assets	7,860,234
Current liabilities	877,798
Equity	\$ 6,982,436
Statement of Operations	
Revenues	\$ -
Expenses	267,710
Net loss	\$ 267,710
Statement of Cash Flows	
Cash provided by (used for)	
Operating activities	\$ (86)
Financing activities	7,250,145
Investing activities	-
Net increase in cash and short-term investments	\$7,250,059

AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements

5. DEFERRED ASSETS

	March 31, 2000 (unaudited)		
	Cost	Accumulated amortization	Net book value
Installation costs	\$ 6,341,501	\$ 3,942,840	\$ 2,398,661
Promotion costs	1,376,701	377,345	999,356
Foreign exchange	1,161,739	839,034	322,705
	<u>\$ 8,879,941</u>	<u>\$ 5,159,219</u>	<u>\$ 3,720,722</u>

	March 31, 1999 (unaudited)		
	Cost	Accumulated amortization	Net book value
Installation costs	\$ 3,497,025	\$ 2,003,237	\$ 1,493,788
Promotion costs	269,820	48,123	221,697
Foreign exchange	1,161,739	451,787	709,952
	<u>\$ 4,928,584</u>	<u>\$ 2,503,147</u>	<u>\$ 2,425,437</u>

	September 30, 1999		
	Cost	Accumulated amortization	Net book value
Installation costs	\$ 5,400,538	\$ 2,794,691	\$ 2,605,847
Promotion costs	551,949	140,548	411,401
Foreign exchange	1,161,739	645,411	516,328
	<u>\$ 7,114,226</u>	<u>\$ 3,580,650</u>	<u>\$ 3,533,576</u>

	September 30, 1998		
	Cost	Accumulated amortization	Net book value
Installation costs	\$ 2,605,248	\$ 1,340,022	\$ 1,265,226
Promotion costs	53,708	5,350	48,358
Foreign exchange	1,161,739	258,164	903,575
	<u>\$ 3,820,695</u>	<u>\$ 1,603,536</u>	<u>\$ 2,217,159</u>

AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements

6. CAPITAL ASSETS

		March 31, 2000 (unaudited)	
	<u>Cost</u>	<u>Accumulated depreciation</u>	<u>Net book value</u>
Telecommunications network	\$ 47,961,287	\$ 1,114,612	\$ 46,846,675
Billing system	10,563,950	1,201,385	9,362,565
Computer hardware and software	13,516,058	2,985,890	10,530,168
Furniture and fixtures	2,818,945	590,826	2,228,119
Leasehold improvements	1,843,804	252,183	1,591,621
Office equipment	714,347	110,378	603,969
Other assets	154,828	51,352	103,476
Office equipment under capital lease	344,427	84,064	260,363
	<u>\$ 77,917,646</u>	<u>\$ 6,390,690</u>	<u>\$ 71,526,956</u>

		March 31, 1999 (unaudited)	
	<u>Cost</u>	<u>Accumulated depreciation</u>	<u>Net book value</u>
Telecommunications network	\$ 17,460	\$ 728	\$ 16,732
Billing system	—	—	—
Computer hardware and software	2,188,847	851,934	1,336,913
Furniture and fixtures	869,833	287,610	582,223
Leasehold improvements	447,658	36,726	410,932
Office equipment	469,303	150,122	319,181
Other assets	70,364	15,803	54,561
Office equipment under capital lease	—	—	—
	<u>\$ 4,063,465</u>	<u>\$ 1,342,923</u>	<u>\$ 2,720,542</u>

		September 30, 1999	
	<u>Cost</u>	<u>Accumulated depreciation</u>	<u>Net book value</u>
Telecommunications network	\$ 13,741,886	\$ —	\$ 13,741,886
Billing system	7,497,469	412,723	7,084,746
Computer hardware and software	5,910,802	1,573,772	4,337,030
Furniture and fixtures	1,883,912	418,168	1,465,744
Leasehold improvements	1,174,347	105,031	1,069,316
Office equipment	748,029	218,495	529,534
Other assets	60,504	21,371	39,133
Office equipment under capital lease	344,427	54,471	289,956
	<u>\$ 31,361,376</u>	<u>\$ 2,804,031</u>	<u>\$ 28,557,345</u>

AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements

6. CAPITAL ASSETS (Continued)

		September 30, 1998	
	Cost	Accumulated depreciation	Net book value
Computer hardware and software	\$ 1,946,838	\$ 692,220	\$ 1,254,618
Furniture and fixtures	766,763	202,146	564,617
Leasehold improvements	127,246	26,987	100,259
Office equipment	446,930	105,032	341,898
Other assets	54,977	10,306	44,671
	<u>\$ 3,342,754</u>	<u>\$ 1,036,691</u>	<u>\$ 2,306,063</u>

7. GOODWILL

	March 31, 2000 1999 (unaudited)		September 30, 1999 1998	
Goodwill net of accumulated amortization and writedown of \$928,205 (September 30, 1999 - \$223,025)	\$25,991,957	\$ —	\$ 7,483,996	\$ —

The Company’s acquisition transactions have been accounted for by the purchase method of accounting under which the assets purchased and the liabilities assumed were recorded at their fair values with the excess of the purchase price over the fair value of the net assets acquired being recorded as goodwill. Under the purchase method, the respective operations of each of the acquisitions are included in the Company’s Consolidated Statements of Operations and Deficit and Cash Flows only from the date of acquisition.

i) Acquisition of Canadian Telecom Resellers Alliance Inc. (“CTRA”)

On June 17, 1999, Axxent Corp. acquired all of the issued and outstanding shares of CTRA, through the acquisition of Oakbrook Communications Inc., for total consideration of \$1,125,000. The consideration paid included \$500,000 cash and the issuance of 1,250,000 warrants (the “CTRA” warrants) to purchase an aggregate 416,667 Class B non-voting shares at an exercise price of \$2.00 per warrant. One quarter of the CTRA warrants become exercisable on each of the following dates: June 17, 1999, December 17, 1999, June 16, 2000 and December 15, 2000. The warrants were valued at \$625,000 on the date of acquisition.

In addition, the Company has agreed to issue 750,000 additional CTRA warrants to purchase 250,000 Class B non-voting shares at an exercise price of \$2.00 per warrant which are contingent on certain performance goals being met as stated in the purchase agreement. If the performance goals are met, the warrants will be exercisable any time after November 30, 2000 and prior to the expiration date of June 17, 2004. No value has been assigned to these CTRA warrants at the date of acquisition as management is not reasonably assured as to the outcome of the contingency.

AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements

On October 1, 1999, CTRA was amalgamated with Axxent Corp. and the amalgamated company continued operations as Axxent Corp.

ii) Acquisition of Pathway Communications (“Pathway”)

On July 29, 1999, Axxent Corp. acquired all of the issued and outstanding shares of 1108108 Ontario Inc., which carried on business as Pathway for a total purchase price of \$7,000,000. The purchase price included shares acquired for cash of \$3,500,000, the issue of an aggregate of 1,250,000 Series 1 and Series 2 preferred shares valued at \$2,500,000, and contingent consideration of \$500,000 cash and special warrants to acquire 83,333 Class B non-voting shares valued at \$500,000 if certain performance goals to be agreed upon by December 31, 1999 were met. In the event that the parties were unable to agree upon such performance goals, Axxent Corp. agreed to pay the vendors of the Pathway shares over an 18 month period \$400,000 and to issue special warrants exercisable, at no additional consideration, for 66,667 Class B non-voting shares valued at \$400,000.

The Series 1 and Series 2 preferred shares were automatically converted into 416,667 Class B non-voting shares on December 14, 1999, following the Ontario Securities Commission’s issuance of a receipt for a (final) prospectus qualifying the distribution of the Class B non-voting shares issued upon conversion of the Series 1 and Series 2 preferred shares.

On December 31, 1999, the parties were unable to agree on performance goals. Under the terms of the agreement, the contingent consideration to be paid will be \$800,000. As a result, as at December 31, 1999, the goodwill has been adjusted to reflect the final purchase price, which is a result of the contingent consideration being finalized. Prior periods have not been restated as the effects of this adjustment are being treated prospectively.

On October 1, 1999, Pathway was amalgamated with Axxent Corp. and the amalgamated company continued operations as Axxent Corp.

iii) Unaudited - Acquisition of EDI Communications Networking Inc. (“EDI”)

On March 23, 2000 the Company acquired all of the issued and outstanding shares of EDI for a purchase price of \$4,850,000 through the issuance of Class B non-voting shares. At closing, 193,516 Class B non-voting shares were issued. Also at closing, \$400,000 of the purchase price was subject to a holdback which, subject to any purchase price adjustments, will be satisfied through the issuance of 17,422 Class B non-voting shares. In addition, the Company may be required to issue further consideration of up to an additional \$5,650,000 in Class B non-voting shares if certain performance targets are met. Pursuant to a purchase agreement dated June 8, 2000, the Company transferred all of the issued and outstanding shares of EDI to Axxent Corp. in exchange for 211,237 common shares of Axxent Corp.

iv) Unaudited - Acquisition of Simcoe County Long Distance Corporation and Quinte Long Distance Corporation (“Simcoe” and “Quinte”)

On March 29, 2000 Axxent Corp. acquired all of the issued and outstanding shares of Simcoe through the acquisition of 1045829 Ontario Limited and all of the issued and outstanding shares of Quinte for a total purchase price of \$15,000,000 cash.

AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements

A summary of the assets and liabilities acquired are as follows:

	CTRA	Pathway	EDI	Simcoe/ Quinte	Total
Cash	\$ 6,331	\$ 340,691	\$ 30,000	\$ 70,283	\$ 447,305
Current assets	80,357	466,016	415,197	950,773	1,912,343
Capital assets	-	887,058	1,474,642	406,915	2,768,615
Current liabilities	(74,703)	(1,287,771)	(1,618,590)	(1,092,361)	(4,073,425)
Net assets acquired at fair value	11,985	405,994	301,249	335,610	1,054,838
Goodwill	1,113,015	6,594,006	4,548,751	14,664,390	26,920,162
Purchase price	\$ 1,125,000	\$ 7,000,000	\$ 4,850,000	\$15,000,000	\$27,975,000

8. RELATED PARTY TRANSACTION

Included in accounts payable and accrued liabilities as at March 31, 2000 (unaudited) is an amount payable to a shareholder of \$1,255,652 (September 30, 1999 - \$nil; September 30, 1998 - \$nil; (unaudited)- March 31, 1999 (unaudited) - \$nil) related to certain DSL equipment purchases. This related party transaction is in the normal course of business and has been recognized in the accounts of the Company at the exchange amount.

9. CAPITAL LEASE OBLIGATIONS

The Company has entered into leases for certain equipment which have been capitalized. The leases that exist at March 31, 2000 expire in 2003 and bear interest at rates ranging from 10.1% to 11.3% per annum. The minimum future lease payments are as follows:

	March 31, 2000 (unaudited)	September 30, 1999
2000	\$ 207,531	\$ 91,068
2001	255,592	91,068
2002	134,248	91,068
2003	91,060	91,060
Total minimum payments	688,431	364,264
Less amount representing interest at varying rates	(83,279)	(74,308)
Present value obligations under capital leases	605,152	289,956
Less: current portion	345,456	60,878
Long term obligations under capital leases	\$ 259,696	\$ 229,078

During the six months ended March 31, 2000 – (unaudited), interest expense relating to the capital lease obligation was \$15,940 (September 30, 1999 - \$36,500; September 30, 1998 - \$nil; March 31, 1999 (unaudited) - \$nil).

AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements

10. SENIOR NOTES PAYABLE

During the 1998 fiscal year, Axxent Corp. issued U.S. \$30,000,000 and CAD \$7,162,250 of senior notes due December 30, 2004. The notes have 7,465,250 detachable warrants to purchase common shares of Axxent Corp. at an issue price of \$0.01 per share and bear interest at the rate of 15%, payable semi-annually. Axxent Corp. has the option to pay its semi-annual interest payment by way of issuing an additional note to the senior note holders under the same terms and conditions as the original note issued in fiscal 1998. During the six months ended March 31, 2000 (unaudited), Axxent Corp. paid approximately \$4,000,000 (September 30, 1999 – \$10,200,000; September 30, 1998 - \$2,000,000; March 31, 1999 (unaudited) - \$3,800,000) in interest by issuing additional notes.

The notes are subject to certain restrictions and covenants. The Company has the option to repay the debt prior to the due date after giving appropriate notice and paying a bonus as defined under the terms of the Agreement.

11. SHARE CAPITAL

a) Authorized

Unlimited number of common shares
 Unlimited number of Class A voting shares
 Unlimited number of Class B non-voting shares
 Unlimited number of preferred shares

b) Issued and outstanding

	<u>Common shares</u>	
	<u>Shares issued</u>	<u>Amount</u>
Balance, September 30, 1998	28,415,000	\$ 4,957,125
Stock options exercised	1,500	1,500
Balance, March 31, 1999 - (unaudited)	28,416,500	4,958,625
Shares converted to Class A	(28,401,500)	(4,958,624)
Balance, September 30, 1999	15,000	1
Shares converted to Class A	(15,000)	(1)
Balance, March 31, 2000 - (unaudited)	0	\$ 0

	<u>Class A voting shares</u>	
	<u>Shares issued</u>	<u>Amount</u>
Balance, September 30, 1998	—	\$ —
Balance, March 31, 1999 - (unaudited)	—	—
Shares issued from conversion of common (i)	9,467,166	4,958,624
Balance, September 30, 1999	9,467,166	4,958,624
Shares issued from special warrants (ii)	5,803,333	32,707,719
Shares issued from conversion of common shares (i)	5,000	1
Shares converted to Class B	(8,274,696)	(25,634,330)
Balance, March 31, 2000 - (unaudited)	7,000,803	\$ 12,032,014

AXXENT INC. (formerly, “OCI Communications Inc.”)
Notes to the Consolidated Financial Statements

11. SHARE CAPITAL (continued)

	<u>Class B non-voting shares</u>	
	<u>Shares issued</u>	<u>Amount</u>
Balance, September 30, 1998	—	\$ —
Balance, March 31, 1999 - (unaudited)	—	—
Stock options exercised	13,317	39,150
Balance, September 30, 1999	13,317	39,150
Shares converted from Class A	8,274,696	25,634,330
Issuance related to IPO (iii)	9,660,000	106,408,425
Shares issued from conversion of preferred shares (i)	416,667	2,500,000
Shares issued (notes 4 and 7)	957,196	12,593,393
Stock options exercised	53,626	145,953
Balance, March 31, 2000 - (unaudited)	19,375,502	\$147,321,251

	<u>Preferred shares</u>	
	<u>Shares issued</u>	<u>Amount</u>
Balance, September 30, 1998	—	\$ —
Balance, March 31, 1999 - (unaudited)	—	—
Shares issued	1,250,000	2,500,000
Balance, September 30, 1999	1,250,000	2,500,000
Shares converted to Class B (i)	(1,250,000)	(2,500,000)
Balance, March 31, 2000 - (unaudited)	—	\$ —

- (i) On October 15, 1999, the Board of Directors approved a share consolidation whereby all of the issued and outstanding Class A voting and Class B non-voting shares would be consolidated on a three-for-one basis. The issued and outstanding share capital has been adjusted to reflect the consolidation of the Class A voting shares and Class B non-voting shares as if the consolidation had occurred at the beginning of the period.
- (ii) During the 1999 fiscal year, the Company issued a total of 17,410,000 special warrants pursuant to an agency agreement, dated April 1999, at a price of \$2.00 per special warrant. The special warrants were exercised for no additional consideration, into 5,803,333 Class A voting shares.
- (iii) On October 28, 1999, the Company completed its Initial Public Offering (“IPO”) of 8,400,000 Class B non-voting shares at a price of \$12.00 per share for a total of \$100,800,000. On December 22, 1999, an Over Allotment Option of 1,260,000 Class B non-voting shares was exercised at a price of \$12.00 per share for a total of \$15,120,000. The total gross proceeds of the IPO was \$115,920,000 and issue costs relating to the IPO were \$9,511,575.

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11. SHARE CAPITAL (continued)

- (iv) As discussed in Note 1, on February 2, 1999, the Company was incorporated in contemplation of a reorganization with Axxent Corp. From February 9, 1999 to April 1, 1999, Optel Communications Inc. issued 28,401,500 Class A voting shares (9,467,166 after the three-for-one share consolidation) in a share for share exchange for common shares of Axxent Corp. Subsequent to this exchange of shares Optel Communications Inc. owned 99.9% of all of the issued and outstanding shares of Axxent Corp.

c) Employee stock options

	Exercise Prices	Number of options
Balance, September 30, 1998		1,313,667
Granted	\$1.50-\$3.00	448,233
Exercised	\$3.00	(1,583)
Balance, March 31, 1999 - (unaudited)		1,760,317
Granted	\$3.00-\$12.00	695,167
Exercised	\$1.50-\$3.00	(11,234)
Balance, September 30, 1999		2,444,250
Granted	\$6.00-\$25.00	1,724,064
Forfeited	\$3.00-\$20.00	(147,307)
Exercised	\$1.50-\$6.00	(53,625)
Balance, March 31, 2000 - (unaudited)		3,967,382

These options were issued to employees of the Company and allow for the purchase of Class B non-voting shares at prices ranging from \$1.50 to \$25.00 and vest over three years. As at March 31, 2000 (unaudited) – 1,523,666 (September 30, 1999 – 1,176,458; March 31, 1999 (unaudited) – 661,500; September 30, 1998 – 258,167) of these options were vested.

d) Warrants

During the fiscal year ended 1998, pursuant to the terms of the senior debt arrangement, the Company issued a total of 7,465,250 detachable warrants to purchase 2,488,417 common voting shares of Axxent Corp. for \$0.03 per share, all of which are outstanding at September 30, 1999. No value has been ascribed to these warrants for financial statement purposes.

During the fiscal year 1999, the Company issued a total of 1,250,000 warrants to purchase 416,667 Class B non-voting shares at an exercise price of \$2.00 per warrant pursuant to the terms of the acquisition of Oakbrook Communications Inc. (note 7i). The warrants were ascribed a value of \$625,000 at the date of acquisition. An additional 750,000 warrants to purchase 250,000 Class B non-voting shares may be exercisable, contingent on certain performance goals (note 7i).

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e) Special warrants

During the fiscal year 1999, the Company issued a total of 17,410,000 special warrants pursuant to an agency agreement, dated April 1999, at a price of \$2.00 per special warrant. The special warrants were exercised for no additional consideration, into 5,803,333 Class A voting shares. Issue costs relating to the special warrants were \$2,112,281.

During the fiscal year 1999, the Company issued special warrants to acquire 83,333 Class B non-voting shares valued at \$500,000 pursuant to the terms of the acquisition of Pathway (note 7ii).

(Unaudited) - Pursuant to an Underwriting Agreement dated on March 28, 2000, the Company issued 10,000,000 special warrants at a price of \$18 per special warrant for a total of \$180,000,000. Each special warrant is exercisable into one Class B non-voting share for no additional considerations. Issue costs relating to the special warrants were \$9,505,007.

12. COMMITMENTS

i) Leases

The Company is committed to minimum annual lease payments under various operating lease agreements for its premises and certain office equipment as follows:

	March 31, 2000 (unaudited)		September 30, 1999	
	Premises	Office Equipment	Premises	Office Equipment
2000	\$ 1,772,268	\$ 793,201	\$ 1,533,655	\$ 811,422
2001	1,666,861	642,628	1,514,675	691,553
2002	1,554,500	125,188	1,461,228	387,873
2003	1,432,300	9,143	1,382,271	10,639
2004	393,329	508	672,687	-
Thereafter	214,489	-	240,753	-
	<u>\$ 7,033,747</u>	<u>\$ 1,570,668</u>	<u>\$ 6,805,269</u>	<u>\$ 1,901,487</u>

ii) Other commitment

In July 1999, the Company entered into an agreement with a third party to provide the Company with software systems required to both provision and manage long distance service. The commitment as at March 31, 2000 (unaudited) is approximately \$1,000,000 (September 30, 1999 - \$1,137,500; September 30, 1998 - \$nil; March 31, 1999 (unaudited) – \$nil).

13. LOSS PER SHARE

Fully diluted loss per share has not been presented as the effects of any convertible privileges would be anti-dilutive.

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14. ECONOMIC DEPENDENCE

Bell Canada is the single source supplier for Centrex lines currently provided by the Company to its customers. Purchases from Bell Canada represented more than 40% at March 31, 2000 (unaudited) (September 30, 1999 – 40%; September 30, 1998 – 40%; March 31, 1999 (unaudited) – 40%) of the Company’s total purchases from external suppliers.

The Company has entered into purchase agreements with Bell Canada for provision of Centrex lines from various Bell Central Offices in Ontario and Quebec. These agreements are generally for five years and the amount purchased under these agreements varies from month to month depending on the level of activity associated with each central office. As at March 31, 2000, (unaudited) the Company had entered into 404 (September 30, 1999 – 397; September 30, 1998 – 211; March 31, 1999 (unaudited) – 217) of these agreements.

15. INCOME TAXES

The reconciliation of the Company’s effective income tax rate for the following periods is as follows:

	Six months ended March 31, <u>2000</u> (unaudited)	<u>1999</u>	Year ended September 30 <u>1998</u>	<u>1997</u>
Net loss for the period	\$ (29,098,989)	\$ (27,249,378)	\$(16,898,006)	\$(4,963,576)
Combined federal and provincial rates	44%	44%	44%	44%
Income tax (benefits) expense based on statutory income tax rate:	(12,803,555)	(11,989,726)	(7,435,123)	(2,183,973)
Deferred charges deductible for tax purposes	(238,143)	(681,457)	(200,450)	(386,231)
Differences resulting from tax values of capital assets	1,699,476	777,630	305,955	122,580
Net financing costs not deducted for tax purposes	–	–	1,335,009	–
Costs relating to issue of Warrants deductible for tax purposes	(92,940)	–	–	–
Goodwill not deductible for tax purposes	331,399	98,130	–	–
Issue costs relating to initial public offering	(418,509)	–	–	–
Other items	–	–	18,514	62,730
Income tax benefit	(11,522,272)	(11,795,423)	(5,976,095)	(2,384,894)
Tax benefit of losses not recognized	11,522,272	11,795,423	5,976,095	2,384,894
Income tax expense	\$ -	\$ -	\$ -	\$ -

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15. INCOME TAXES (Continued)

	March 31, 2000 (unaudited)	1999	September 30, 1998	1997
Future income tax assets				
Capital assets	\$ 3,837,235	\$ 1,209,892	\$ 432,262	\$ 150,497
Non capital losses	33,863,091	21,164,360	9,183,056	3,206,961
Financing fees	1,024,279	1,001,257	1,335,009	—
Issue costs for warrants and IPO	4,196,146	—	—	—
Valuation allowance	(41,425,623)	(22,127,434)	(10,383,709)	(2,991,290)
Future income tax liabilities				
Deferred Charges	(1,495,128)	(1,248,075)	(566,618)	(366,168)
Total	\$ —	\$ 0	\$ 0	\$ 0

As at September 30, 1999, the Company has non-capital losses of approximately \$47,200,000 available to reduce future years' income for tax purposes, the tax effect of which has not been recorded in these consolidated financial statements.

If not utilized, these losses will expire as follows:

2002	\$ 300,000
2003	1,500,000
2004	5,400,000
2005	13,000,000
2006	27,000,000
	\$ 47,200,000

Losses incurred in the six month period ended March 31, 2000 have not been included in the above calculation.

16. RISK MANAGEMENT

The Company is exposed to the following risks related to financial assets and liabilities:

Credit risk

Credit risk arises from the possibility that the Company's customers may experience financial difficulty and be unable to fulfill their financial obligations. This risk is mitigated by the fact that the Company has a large number of diverse customers which minimizes concentration of credit risk. The Company also manages this risk through proactive credit screening and a stringent collection policy.

Foreign exchange risk

The Company has issued U.S. \$30,000,000 in senior notes with principal and interest payable in US dollars. This exposes the Company to foreign exchange risk. The Company manages this risk

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through the purchase of a foreign exchange contract to hedge the principal re-payment of U.S. \$30,000,000. The Company has issued further U.S. dollar denominated senior notes (note 10) which are not hedged by a foreign exchange contract.

17. UNCERTAINTY DUE TO THE YEAR 2000 ISSUE

The Year 2000 Issue arises because many computerized systems use two digits rather than four to identify a year. Date-sensitive systems may recognize the year 2000 as 1900 or some other date, resulting in errors when information using year 2000 dates is processed. In addition, similar problems may arise in some systems which use certain dates in 1999 to represent something other than a date. Although the change in date has occurred, it is not possible to conclude that all aspects of the Year 2000 Issue that may affect the Company, including those related to customers, suppliers, or other parties, have been fully resolved.

18. SUBSEQUENT EVENTS

i) Unaudited – Related party transaction

On April 11, 2000, the Company made a non-interest bearing loan in the amount of \$75,000 to a director of the Company in the form of a promissory note due April 11, 2001.

ii) Unaudited - Acquisition

On May 4, 2000, the Company purchased all of the issued and outstanding shares of Optimum Teleservices Inc. (“OTI”) for a total purchase price of \$5,400,000 comprised of \$2,700,000 in cash consideration and \$2,700,000 in equity consideration through the issuance of an additional 173,188 Class B non-voting shares of the Company. The purchase price is subject to certain adjustments. This acquisition will be accounted for by the purchase method.

iii) Unaudited - Employee stock options

Subsequent to March 31, 2000, as of May 15, 2000 the Company granted 280,723 stock options under the Employee Stock Option Plan.

19. COMPARATIVE FIGURES

Certain of the comparative figures have been reclassified to conform with the current period’s financial statement presentation.

GLOSSARY

“ADSL” – asymmetric digital subscriber line, DSL technology that is asymmetric in that it provides for more bandwidth downstream, from a network service provider’s office to the customer site, than upstream from the customer to the central office.

“ADSL lite” – a lower speed version of ADSL technology that does not require the installation of equipment at the customer premises.

“ATM” – asynchronous transfer mode, a switching technology that allows voice, data, image and video traffic to be combined into evenly sized cells for high-speed transmission over one access circuit.

“backbone network” – the major transmission path for network interconnection.

“Building Access Decision” – Telecom Decision CRTC 99-10, *Location of Demarcation Point for Inside Wire in Multi-Dwelling Units and Associated Issues*, the decision of the CRTC dated August 6, 1999 which established guidelines for access by carriers to multi-tenant buildings.

“carriers” – a Canadian facilities-based provider of telecommunications services.

“Central Office” – the switching centres or central switching facilities of a carrier.

“Centrex” – is a switching system located at a LEC’s central office which allows calls from the outside to be routed directly to the individual instead of through central exchange. Centrex duplicates the functions and services of a PBX.

“CLEC” – a competitive local exchange carrier, that provides connections for local voice and data services in competition with the ILECs.

“Co-location” – the ability of a CLEC to connect its network to the ILEC’s Central Offices. Physical co-location occurs when a CLEC places its equipment inside the ILEC’s central office.

“CRTC” – the Canadian Radio-television and Telecommunications Commission, an independent federal government authority responsible for the regulation of telecommunications and broadcasting in Canada.

“DSL” – digital subscriber line, a local loop access technology which allows multiple forms of data, voice and video to be carried over the local loop between a network service provider’s central office and the customer site.

“e-commerce” – electronic commerce.

“FDDI” – fibre distributed data interface, that is used in connection with optical-fibre based token-rings networks and features dual counter-rotating rings, each with a data transmission capacity of 100 million bits per second.

“Frame Relay Services” – high-speed data services for switched-data communications between computers.

“ILEC” – the incumbent local exchange carrier which, prior to the opening of competition in the Canadian telecommunications industry, had a monopoly for local and long distance telecommunications services in a specified region in Canada.

“Intranet” – a private network that uses Internet software and standards.

“ISDN” – integrated services digital network, provides end-to-end digital connectivity for simultaneous transmission of voice and data on internationally defined standards and is used to access the Internet.

“ISP” – Internet service provider.

“LEC” – local exchange carrier.

“LNP” – local number portability, which allows customers to receive local services from a different LEC without changing phone numbers.

“Local Competition Decision” – Telecom Decision CRTC 97-8, *Local Competition*, the decision of the CRTC dated May 1, 1997 which opened Canada’s local telecommunications services market to switch-based competition effective January, 1998.

“local loop” – the physical connection between a customer’s premises and a LEC’s Central Office comprising, primarily, the copper wire.

“POP” – a long distance provider’s point-of-presence which is the physical location at which the interconnection between the networks of the long distance provider and a LEC is made.

“PBX” – private branch exchange trunks, is a switching system within an office building which allows calls from outside to be routed directly to the individual instead of through a central exchange;

“Price Cap Decision” – Telecom Decision CRTC 97-9, *Price Cap Regulation and Related Issues*, the decision of the CRTC dated May 1, 1997 which adopted a form of price cap regulation for the ILECs.

“Rate-Adaptive DSL (R-ADSL)” – rate-adaptive digital subscriber line, DSL technology that operates within similar DSL technology transmission rates as ADSL, but adjust to varying lengths and qualities of local access lines.

“Sonet technology” – synchronous optical network, an ultra high-speed fibre optic transmission standard for large scale fibre-based digital transmission networks.

“switch” – a sophisticated computer that accepts instructions from a caller in the form of a telephone number which tells the switch where to route the call.

“T-1” – a 1.544 million bits per second line.

“wide area network (WAN)” – a geographic dispersed network.

CERTIFICATE OF THE COMPANY

Dated: June 12, 2000

The foregoing constitutes full, true and plain disclosure of all material facts relating to the securities offered by this prospectus as required by Part XV of the *Securities Act* (Ontario), by Part 8 of the *Securities Act* (Alberta), by Part VII of the *Securities Act* (Manitoba) and the respective regulations thereunder. This prospectus, as required by the *Securities Act* (Québec) and the regulations thereunder, does not contain any misrepresentation that is likely to affect the value or the market price of the securities to be distributed.

ROBERT LATHAM
Chief Executive Officer

CHRISTOPHER CLINNING
Chief Financial Officer

On behalf of the Board of Directors

PERRY DELLELCE
Director

STEPHEN R. COXFORD
Director

CERTIFICATE OF THE UNDERWRITERS

Dated: June 12, 2000

To the best of our knowledge, information and belief, the foregoing constitutes full, true and plain disclosure of all material facts relating to the securities offered by this prospectus as required by Part XV of the *Securities Act* (Ontario), by Part 8 of the *Securities Act* (Alberta), by Part VII of the *Securities Act* (Manitoba) and the respective regulations thereunder. To our knowledge, this prospectus, as required by the *Securities Act* (Québec) and the regulations thereunder, does not contain any misrepresentation that is likely to affect the value or the market price of the securities to be distributed.

GRIFFITHS MCBURNEY & PARTNERS

By: J. ROBERT FRASER

CIBC WORLD MARKETS INC.

By: BLAKE CORBET

SCOTIA CAPITAL INC.

By: JOHN FARIS

CREDIT SUISSE FIRST BOSTON
SECURITIES CANADA INC.

By: BRIAN IMRIE

YORKTON SECURITIES INC.

By: NELSON SMITH