Consolidated Financial Statements

CityXpress Corp.

(Expressed in U.S. dollars)
June 30, 2003 and 2002

Grant Thornton LLP
Chartered Accountants
Management Consultants
Canadian Member of
Grant Thornton International

REPORT OF INDEPENDENT AUDITORS

To the Shareholders of
CityXpress Corp.

We have audited the accompanying consolidated balance sheets of **CityXpress Corp.** as of June 30, 2003 and 2002, and the related consolidated statements of operations, stockholders' deficiency and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about 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. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of CityXpress Corp. at June 30, 2003 and 2002 and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the financial statements, the Company has incurred recurring operating losses and has a working capital deficiency. The Company is dependent on its ability to raise capital from shareholders or other sources to sustain operations. These factors, along with other matters set out in Note 1, raise substantial doubt that the Company will be able to continue as a going concern. Management's plans in regard to these matters are also described in Note 1. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

Grant Thornton LLP

Vancouver, Canada,
August 15, 2003

Chartered Accountants

CityXpress Corp.

CONSOLIDATED BALANCE SHEETS

[See Nature of Operations and Basis of Presentation - Note 1]

As at June 30 (Expressed in U.S. dollars)

	2003 $	2002 $
ASSETS *[note 11]*		
Current		
Cash and cash equivalents	**12,308**	82,974
Accounts receivable, net of allowance for doubtful accounts of $nil in 2003 and 2002 *[note 4]*	**94,169**	3,091
Other receivables	**7,132**	4,288
Prepaid expenses and other	**26,603**	16,329
Total current assets	**140,212**	106,682
Property and equipment *[note 5]*	**124,465**	102,232
Product development costs *[note 6]*	**171,579**	149,634
Intangible assets *[note 7]*	**53,492**	—
Total assets	**489,748**	358,548
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current		
Accounts payable *[note 8]*	**291,423**	209,200
Accrued liabilities *[note 8]*	**421,423**	244,196
Deferred revenue	**250,763**	11,266
Revolving loan *[note 9]*	**66,790**	—
Current portion of loans payable *[note 10]*	**350,000**	350,000
Convertible loan debentures *[note 11]*	**3,300,000**	—
Demand instalment loan *[note 12]*	—	152,910
Stockholders' loans *[note 13]*	**611,942**	272,836
Current portion of obligations under capital leases *[note 14]*	**70,812**	29,357
Total current liabilities	**5,363,153**	1,269,765
Obligations under capital leases *[note 14]*	**47,773**	40,030
Convertible loan debentures *[note 11]*	—	3,000,000
Total liabilities	**5,410,926**	4,309,795
Commitments *[note 15]*		
Stockholders' deficiency		
Share capital *[note 16]*		
Common stock - $0.001 par value Authorized shares: 100,000,000 Issued and outstanding: 24,520,033 at June 30, 2003 and 23,303,898 at June 30, 2002	**24,520**	23,304
Common stock to be issued – 198,587 at June 30, 2003 and nil at June 30, 2002	**12,650**	—
Additional paid in capital	**5,984,090**	5,843,305
Accumulated other comprehensive income	**19,625**	19,625
Deficit	**(10,962,063)**	(9,837,481)
Total stockholders' deficiency	**(4,921,178)**	(3,951,247)
Total liabilities and stockholders' deficiency	**489,748**	358,548

See accompanying notes

CityXpress Corp.

CONSOLIDATED STATEMENTS OF OPERATIONS

[See Nature of Operations and Basis of Presentation - Note 1]

Years ended June 30 (Expressed in U.S. dollars)

	2003 $	2002 $
Revenue *[note 4]*		
Auctions	**784,963**	66,200
Special Sections	**388,518**	348,330
Total revenues	**1,173,481**	414,530
Cost of sales (including amortization of product development costs of $99,749, 2002 - $55,187)	**467,841**	581,639
Gross profit (loss)	**705,640**	(167,109)
Operating expenses		
Sales and marketing	**552,770**	439,882
Product development and technology	**410,919**	382,186
Finance and administration	**578,386**	479,875
Amortization of eCommerce technology	**—**	275,334
	1,542,075	1,577,277
Operating loss	**(836,435)**	(1,744,386)
Other income (expense)		
Interest expense	**(173,261)**	(165,467)
Interest and miscellaneous income	**63**	78
Foreign exchange loss	**(114,949)**	(12,769)
Total other expense	**(288,147)**	(178,158)
Loss before income taxes	**(1,124,582)**	(1,922,544)
Deferred income tax recovery *[note 17]*	**—**	93,100
Net loss and comprehensive loss for the year	**(1,124,582)**	(1,829,444)
Net loss per common share *[note 16[d]]*		
Basic and diluted	**(0.05)**	(0.08)
Weighted average number of common shares *[note 16[d]]*		
Basic and diluted	**24,194,083**	23,222,231

See accompanying notes

CityXpress Corp.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' DEFICIENCY

[See Nature of Operations and Basis of Presentation - Note 1]

(Expressed in U.S. dollars)

	Common stock #	Common stock to be issued #	Common stock issued and outstanding $	Common stock to be issued $	Additional paid in capital $	Accumulated other comprehensive income $	Deficit $	Total stockholders' equity (deficit) $
Year ended June 30, 2002								
Balance at June 30, 2001	23,043,898	—	23,044	—	5,813,315	19,625	(8,008,037)	(2,152,053)
Shares issued on exercise of warrants	100,000	—	100	—	24,900	—	—	25,000
Shares issued for services rendered	160,000	—	160	—	4,640	—	—	4,800
Stock based compensation	—	—	—	—	450	—	—	450
Net loss for the year	—	—	—	—	—	—	(1,829,444)	(1,829,444)
Balance at June 30, 2002	23,303,898	—	23,304	—	5,843,305	19,625	(9,837,481)	(3,951,247)
Acquisition of 10digit communications *[notes [7] and 16[a]]*	1,216,135	—	1,216	—	60,141	—	—	61,357
Shares to be issued *[note 16(a)]*	—	198,587	—	12,650	—	—	—	12,650
Stock based compensation *[note 13(b)(iii) and (iv)]*	—	—	—	—	80,644	—	—	80,644
Net loss for the year	—	—	—	—	—	—	(1,124,582)	(1,124,582)
Balance at June 30, 2003	24,520,033	198,587	24,520	12,650	5,984,090	19,625	(10,962,063)	(4,921,178)

See accompanying notes

CityXpress Corp.

CONSOLIDATED STATEMENTS OF CASH FLOWS

[See Nature of Operations and Basis of Presentation - Note 1]

Years ended June 30 (Expressed in U.S. dollars)

	2003 $	2002 $
OPERATING ACTIVITIES		
Net loss for the year	**(1,124,582)**	(1,829,444)
Adjustments to reconcile net loss to net cash used in operating activities:		
Amortization	**21,450**	275,334
Depreciation	**178,694**	110,851
Shares to be issued for services rendered	**12,650**	**—**
Shares issued for services rendered	**—**	4,800
Stock based compensation	**80,644**	450
Deferred income tax recovery	**—**	(93,100)
Deferred revenue	**239,497**	10,752
Changes in operating assets and liabilities:		
Accounts receivable	**(91,078)**	15,996
Other receivables	**(2,844)**	2,904
Prepaid expenses and other	**(10,274)**	7,318
Accounts payable	**82,223**	50,259
Accrued liabilities	**177,227**	107,231
Net cash used in operating activities	**(436,393)**	(1,336,649)
INVESTING ACTIVITIES		
10digit Communications acquisition costs *[note 7]*	**(13,585)**	**—**
Purchase of property and equipment	**(12,292)**	(8,964)
Development costs	**(121,694)**	(122,886)
Net cash used in investing activities	**(147,571)**	(131,850)
FINANCING ACTIVITIES		
Proceeds from revolving loan	**66,790**	**—**
Proceeds from loans payable	**—**	60,000
Proceeds from convertible loan debentures	**300,000**	1,500,000
Repayment of demand instalment loan	**(152,910)**	(8,920)
Repayments under capital leases	**(39,688)**	(20,471)
Proceeds from stockholders' loans	**284,172**	**—**
Repayment of stockholders' loans	**(9,856)**	(11,410)
Net cash provided by financing activities	**448,508**	1,519,199
Effect of foreign exchange rate changes on cash	**64,790**	**—**
Net (decrease) increase in cash and cash equivalents during the year	**(70,666)**	50,700
Cash and cash equivalents, beginning of year	**82,974**	32,274
Cash and cash equivalents, end of year	**12,308**	82,974
Non cash financing and investing transactions not included in cash flows:		
Settlement of accounts payable through the issuance of shares	**—**	25,000
Capital assets acquired through the assumption of capital leases	**88,886**	31,689
Shares issued to acquire 10digit Communications	**61,357**	**—**
Supplemental disclosure		
Interest paid	**47,535**	50,265

See accompanying notes

CityXpress Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2003 and 2002 (Expressed in U.S. dollars)

1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

CityXpress Corp. ("Company") is incorporated under the laws of the State of Florida.

The Company has developed a suite of online products that provide newspapers with solutions through which they can defend and extend their position as the dominant means for local advertisers to promote themselves to local consumers. The Company's online special section product integrates niche editorial content with advertising and promotional tools that leverage a newspaper's brand and traffic. The Company's auction product allows newspapers to auction advertising clients' products in exchange for advertising credits with the newspaper, with the newspaper retaining the cash from all products that are sold in the auction. The Company intends to build further alliances with media companies who own newspaper and television stations. The Company currently operates in only one industry segment and its marketing efforts are currently targeted to the North American market.

The consolidated financial statements for the year ended June 30, 2003 have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business for the foreseeable future. The Company incurred a net loss of $1,124,582 for the year ended June 30, 2003 and has a working capital deficiency of $5,222,941 and an accumulated deficit of $10,962,063 at June 30, 2003. These factors raise substantial doubt about the Company's ability to continue as a going concern. The ability of the Company to continue as a going concern is dependent upon its ability to achieve profitable operations and to obtain additional capital. Management expects to raise additional capital through private placements and other types of venture fundings and through financing agreements with its clients. Also, management expects to generate higher revenues over the 2004 fiscal year. The outcome of these matters cannot be predicted at this time. No assurances can be given that the Company will be successful in raising sufficient additional capital or increasing revenues. Further, there can be no assurance, assuming the Company successfully raises additional funds or increases evenues, that the Company will achieve positive cash flow. If the Company is unable to obtain adequate additional financing or additional revenues, management will be required to curtail the Company's operating expenses. These consolidated financial statements do not include any adjustments to the specific amounts and classifications of assets and liabilities which might be necessary should the Company be unable to continue in business.

2. SIGNIFICANT ACCOUNTING POLICIES

The consolidated financial statements have been prepared by management in accordance with accounting principles generally accepted in the United States of America. The Company's significant accounting policies are summarized below

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd)

Principles of consolidation

The consolidated financial statements include the accounts of CityXpress Corp. and its wholly-owned subsidiaries: WelcomeTo Search Engine Inc. (British Columbia, Canada) and Xceedx Technologies Inc. (British Columbia, Canada). All significant intercompany balances and transactions have been eliminated on consolidation.

Cash equivalents

The Company considers all highly liquid financial instruments purchased with an original maturity of three months or less to be cash equivalents. Cash equivalents are recorded at cost, which approximates market value.

Leases

Leases are classified as either capital or operating leases. Leases which transfer substantially all the benefits and risks of ownership of the property to the Company are accounted for as capital leases. Capital lease obligations reflect the present value of future lease payments, discounted at the appropriate interest rate. All other leases are accounted for as operating leases whereby rental payments are expensed as incurred.

Property and equipment

Property and equipment are recorded at cost. Depreciation is computed on the straight-line method over the estimated useful life of the assets as follows:

Computer equipment and software	3 years
Office furniture and equipment	5 years
Leasehold improvements	Lease term

Computer equipment acquired under capital leases is also depreciated on the straight-line method over the shorter of the lease term and the estimated useful life on the asset.

Product development costs

Product development costs incurred after technological feasibility of a product has been established are capitalized until the developed product is available for general release.

Product development costs are amortized on the straight-line method over a 3 year period.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Intangible assets

Intangible assets arose as part of the acquisition of 10digit Communications and is being amortized on the straight-line method over its useful life, which is 36 months.

The estimated amortization expense related to the Company's intangible assets over the next five years is:

2004	$24,981
2005	$24,981
2006	$3,530
2007	$ Nil
2008	$ Nil

Website development costs

Website development costs are charged to expense as incurred unless the development costs meet the criteria under generally accepted accounting principles for deferral and amortization. The Company has not deferred any website development costs to date.

Impairment of long-lived assets

The Company monitors the recoverability of long-lived assets, including capital and intangible assets, based upon estimates using factors such as future asset utilization, business climate and future non-discounted cash flows expected to result from the use of the related assets or to be realized on sale. The Company's policy is to write down assets to their fair value in the year when it is determined likely that the carrying amount of the asset will not be recovered.

Stock-based compensation

The Company has adopted the disclosure-only provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, *"Accounting for Stock-Based Compensation"* for stock options granted to employees.

Stock options granted to non-employees are accounted for under SFAS No. 123 using the fair value method. Compensation expense is calculated using the Black Scholes option pricing model and recorded over the period the services are rendered.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Stock options

The weighted average fair value of options granted during the year ended June 30 was as follows:

	Options #	Weighted average fair value $
2003		
Exercise price:		
Greater than fair market value	310,000	0.10
	310,000	0.10
2002		
Exercise price:		
Greater than fair market value	1,370,000	0.05
	1,370,000	0.05

Pro forma information regarding net income and earnings per share is required by Statement of Financial Accounting Standard ("SFAS") No. 123, which also requires that the information be determined as if the Company had accounted for its employee stock options under the fair value method of that statement. The fair value of each option granted during the year was estimated at the date of grant using the Black-Scholes pricing model with the following weighted average assumptions: risk free interest rates of 5% [2001 - 5%]; dividend yields of nil; volatility factors of the expected market price of the Company's common stock of 140% [2002 – 170%] and a weighted average expected life of the option of 4.00 years [2002 – 2.79 years].

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the vesting period. The Company's pro forma information for the year ended June 30, is as follows:

		2003 $	2002 $
Net loss	As reported	**(1,124,582)**	(1,829,444)
SFAS 123 compensation expense	Pro forma	**(31,000)**	(49,700)
Pro forma net loss attributable to common stockholders	Pro forma	**(1,155,582)**	(1,879,144)
Weighted average number of common shares outstanding		**24,194,083**	23,222,231
Pro forma net loss per common share:			
Basic and diluted	Pro forma	**(0.05)**	(0.08)

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Capital stock issued for consideration other than cash

Capital stock issued for consideration other than cash is recorded at an estimate of the fair value of the stock issued or issuable or at an estimate of the fair value of the goods or services received (whichever is more readily ascertainable).

Foreign currency translation

Until March 31, 2000, the functional currency of the Company was the Canadian dollar, while the reporting currency in the consolidated financial statements was the U.S. dollar. Consolidated asset and liability accounts were translated into U.S. dollars at the exchange rate in effect at the balance sheet date. Consolidated revenue and expense amounts were translated at the average exchange rate for the period. Gains or losses resulting from this process were recorded in stockholders' equity as an adjustment to accumulated other comprehensive income.

Effective April 1, 2000, the functional currency of the Company and its subsidiaries changed to the U.S. dollar. Accordingly, for the Canadian subsidiaries, monetary assets and liabilities are translated into U.S. dollars at exchange rates prevailing at the balance sheet date and non-monetary items are translated at exchange rates prevailing at the historic rate. Revenue and expenses are translated at the average exchange rate for the year. Gains or losses arising on this foreign currency translation are recorded in income.

Revenue recognition

The Company enters into sales contracts that may encompass multiple elements, including advertising and promotional fees, editorial content fees, training fees, custom development fees and auction fees. Revenue for the various elements are allocated based on their relative fair value. Advertising and promotional, and editorial content fees are recognized monthly as the services are performed. Custom development fees are recognized when the client's web site is activated for the world wide web, at which time the Company retains no material conditions or obligations to the customer. Training fees are recognized as the services are performed. Cash received in advance of services rendered is recorded as deferred revenue.

Auction fees are recognized on completion of the auction per customer newspaper. The Company receives a unit fee per auction article and a percentage of total auction revenue received by the newspaper

Allowance for doubtful accounts

The Company establishes an allowance for doubtful accounts through review of open accounts, and historical collection and allowances amounts. The allowance for doubtful accounts is intended to reduce trade accounts receivable to the amount that reasonably approximates their fair value due to their short-term nature. The amount ultimately realized from trade accounts receivable may differ from the amount estimated in the financial statements based on collection experience and actual returns and allowances.

Advertising costs

Advertising costs are expensed as incurred and amounted to $53,471 in the year ended June 30, 2003 [2002 - $58,398].

Income taxes

The Company uses the liability method of accounting for income taxes. Under this method, deferred tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the enacted tax rates and laws that are expected to be in effect when the differences are expected to reverse. Recognition of deferred tax assets is limited to amounts considered by management to be more likely than not of realization in future periods.

Loss per common share

The basic loss per common share is computed by dividing net loss available to common stockholders by the weighted average number of common shares outstanding for the year. Diluted loss per common share is computed giving effect to all potential dilutive options and warrants that were outstanding during the year. For the years ended June 30, 2003 and 2002, all outstanding options and warrants were anti-dilutive.

Recent pronouncements

Accounting for Costs Associated with Exit or Disposal Activities

In June 2002, the FASB issued Statement 146, Accounting for Costs Associated with Exit or Disposal Activities. This statement requires entities to recognize costs associated with exit or disposal activities when liabilities are incurred rather than when the entity commits to an exit or disposal plan, as currently required. Examples of costs covered by this guidance include one-time employee termination benefits, costs to terminate contracts other than capital leases, costs to consolidate facilities or relocate employees, and certain other exit or disposal activities. This statement is effective for fiscal years beginning after December 31, 2002, and will impact any exit or disposal activities the Company initiates after that date.

Stock-Based Employee Compensation

In December 2002, the FASB issued Statement 148 (SFAS 148), *Accounting for Stock-Based Compensation — Transition and Disclosure: an amendment of FASB Statement 123* (SFAS 123), to provide alternative transition methods for a voluntary change to the fair value based method of accounting for stock-based employee compensation. In addition, SFAS 148 amends the disclosure requirements of SFAS 123 to require prominent disclosures in annual financial statements about the method of accounting for stock-based employee compensation and the pro forma effect on reported results of applying the fair value based method for entities that use the intrinsic value method of accounting. The pro forma effect disclosures are also required to be prominently disclosed in interim period financial statements. This statement is effective for financial statements for fiscal years ending after December 15, 2002 and is effective for financial reports containing condensed financial statements for interim periods beginning after December 15, 2002, with earlier application permitted. The Company does not plan a change to the fair value based method of accounting for stock-based employee compensation and has included the disclosure requirements of SFAS 148 in the accompanying financial statements

Accounting for Guarantees

In November 2002, FASB Interpretation 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others* (FIN 45), was issued. FIN 45 requires a guarantor entity, at the inception of a guarantee covered by the measurement provisions of the interpretation, to record a liability for the fair value of the obligation undertaken in issuing the guarantee. The Company previously did not record a liability when guaranteeing obligations unless it became probable that the Company would have to perform under the guarantee. FIN 45 applies prospectively to guarantees the Company issues or modifies subsequent to December 31, 2002, but has certain disclosure requirements effective for interim and annual periods ending after December 15, 2002. The Company does not anticipate FIN 45 will have a material effect on its 2003 financial statements.

Variable Interest Entities

In January 2003, the FASB issued FASB Interpretation 46 (FIN 46), *Consolidation of Variable Interest Entities*. FIN 46 clarifies the application of Accounting Research Bulletin 51, *Consolidated Financial Statements*, for certain entities that do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties or in which equity investors do not have the characteristics of a controlling financial interest ("variable interest entities"). Variable interest entities within the scope of FIN 46 will be required to be consolidated by their primary beneficiary. The primary beneficiary of a variable interest entity is determined to be the party that absorbs a majority of the entity's expected losses, receives a majority of its expected returns, or both. FIN 46 applies immediately to variable interest entities created after January 31, 2003, and to variable interest entities in which an enterprise obtains an interest after that date. It applies in the first fiscal year or interim period beginning after June 15, 2003, to variable interest entities in which an enterprise holds a variable interest that it acquired before February 1, 2003. The Company is in the process of determining what impact, if any, the adoption of the provisions of FIN 46 will have upon its financial condition or results of operations.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Revenue Recognition

In November 2002, the Emerging Issues Task Force reached a consensus opinion on EITF 00-21, "Revenue Arrangements with Multiple Deliverables." The consensus provides that revenue arrangements with multiple deliverables should be divided into separate units of accounting if certain criteria are met. The consideration for the arrangement should be allocated to the separate units of accounting based on their relative fair values, with different provisions if the fair value of all deliverables are not known or if the fair value is contingent on delivery of specified items or performance conditions. Applicable revenue recognition criteria should be considered separately for each separate unit of accounting. EITF 00-21 is effective for revenue arrangements entered into in fiscal periods beginning after June 15, 2003. Entities may elect to report the change as a cumulative effect adjustment in accordance with APB Opinion 20, Accounting Changes. The Company believes its revenue recognition policies are consistent with this new standard.

Consideration Received from a Vendor

In November 2002 the Emerging Issues Task Force reached a consensus opinion on EITF 02-16, "Accounting by a Customer (including a reseller) for Certain Consideration Received from a Vendor." EITF 02-16 requires that cash payments, credits, or equity instruments received as consideration by a customer from a vendor should be presumed to be a reduction of cost of sales when recognized by the customer in the income statement. In certain situations, the presumption could be overcome and the consideration recognized either as revenue or a reduction of a specific cost incurred. The consensus should be applied prospectively to new or modified arrangements entered into after December 31, 2002. The Company has not yet determined the effects of EITF 02-16 on its financial statements.

3. FINANCIAL INSTRUMENTS

Amounts reported for cash and cash equivalents, accounts receivable, other receivables, accounts payable and accrued liabilities, revolving loan and stockholders' loans approximate their fair values due to the relatively short term nature or demand nature of the instruments. The carrying value of the demand instalment loan, loans payable, loan debentures and obligations under capital leases approximate fair value due to variable interest rates being charged on outstanding balances.

4. CREDIT RISK AND OTHER

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist principally of accounts receivable. The Company performs ongoing credit evaluations of its customers and maintains allowances for potential credit losses which, when realized, have been within range of management's expectations.

For the year ended June 30, 2003, approximately 24% (2002- 57%) of the Company's total revenues were generated through sales to Lee Enterprises Incorporated. At June 30, 2003, approximately 2% of the Company's accounts receivable balance was due from this customer (2002 – nil%).

5. PROPERTY AND EQUIPMENT

	2003		2002	
	Cost $	**Accumulated depreciation** $	**Cost** $	**Accumulated depreciation** $
Computer equipment and software	**175,383**	**156,003**	165,534	140,040
Computer equipment under capital leases	**184,966**	**91,163**	96,081	33,907
Office furniture and equipment	**22,802**	**12,170**	20,853	7,814
Leasehold improvements	**8,189**	**7,539**	7,692	6,167
	391,340	**266,875**	290,160	187,928
Net book value	**124,465**		102,232	

6. PRODUCT DEVELOPMENT COSTS

	2003 $	**2002** $
Cost	**342,902**	221,208
Accumulated depreciation	**171,323**	71,574
	171,579	149,634

7. ACQUISITION

On July 10, 2002, the Company completed the acquisition of 10digit Communications ("10digit"), the online auction division of the Winnipeg Free Press owned by FP Canadian Newspapers Limited Partnership. 10digit was acquired to facilitate expansion of the company's auction business. The purchase price for the acquisition was calculated on revenue recognized from current 10digit customers for 2002 and was satisfied through the issuance of CityXpress shares. The first tranche of 1,004,277 common shares was issued on September 9, 2002 based on revenue generated by 10 digit auctions for the first six month of 2002 and the shares were recorded at their fair value on the date of issuance.

The final tranche of 211,858 common shares was issued to FP Canadian Newspapers Limited Partnership in February 10, 2003 based on revenue generated from existing 10digit auction customers for the final six months of 2002. These shares were recorded at their fair value on the date of issuance.

7. ACQUISITION (cont'd)

The net identifiable assets of 10digit acquired from FP Canadian Newspaper Limited Partnership

during the year ended June 30, 2003 were:

Equipment	$38,834
Intellectual property and contracts	74,942
	$113,776

1,216,135 shares issued	$61,357
Capital leases assumed	38,834
Acquisition costs	13,585
	$113,776

The results of operations of 10digit are included for the period July 10, 2002 to June 30, 2003.

As part of the acquisition, CityXpress also entered into the following agreements with FP Newspapers Limited Partnership:

- a Noncompete and Nonsolicitation Agreement,
- a Registration Rights Agreement,
- an Assignment of Intellectual Property, and
- an Assignment and Assumption of Contracts Agreement.

If this acquisition had occurred on July 1, 2002 or July 1, 2001, the following proforma results of operations have been estimated:

	Year Ended June 30 2003 $	Year Ended June 30 2002 $
Revenue	1,173,481	614,530
Net Loss		(1,124,582)
(1,922,432)		
Net Loss per share (Basic and Diluted)	(0.05)	(0.08)

	2003 $	**2002** $
Intangible assets	**74,942**	—
Accumulated amortization	**21,450**	—
	53,492	**—**

8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	2003	**2002**

	$	$
Trade accounts payable	**291,423**	209,200
Accrued interest	**314,462**	188,676
Accrued vacation	**52,317**	33,341
Accrued liabilities	**54,644**	22,179
Total Accrued liabilities	**421,423**	244,196

9. REVOLVING LOAN

On May 1, 2003, the Company entered into a Revolving Loan and General Security Agreement with a company controlled by a director. Under this agreement, the Company has received $90,000 Cdn ($66,790 US) in funding. The revolving loan carries an interest rate of 10% per annum of the outstanding balance and is payable monthly. The outstanding balance of the loan cannot exceed 90% of the Company's 90 days accounts receivable outstanding balance. Under the General Security Agreement, the Company has pledged its accounts receivable and tangible assets as collateral and security for all loan advances outstanding. Interest for the year ended June 30, 2003 on this loan amounted to $993.

10. LOANS PAYABLE

On August 16, 2000, the Company entered into a Loan and Security Agreement with Lee Enterprises Incorporated ("Lee"). Under this agreement, the Company has received $350,000 in funding in the form of promissory notes that bear interest at the monthly Wall Street Journal rate, as detailed below:

Loan date	**Amount** $	**Maturity date**	**Weighted average effective interest rate (%) for the year ended June 30, 2003**
August 17, 2000	125,000	October 31, 2003	4.40
August 28, 2000	125,000	October 31, 2003	4.40
September 19, 2000	40,000	October 31, 2003	4.40
July 12, 2001	60,000	October 31, 2003	4.40
	350,000		

Pursuant to an Investment Agreement [note 11], the maturity dates of these loans payable were extended from November 17, 2000, November 28, 2000 and December 19, 2000 respectively, to October 31, 2003. Interest payable on these loans is payable on demand.

In conjunction with these agreements, the Company entered into a Collateral License Agreement and Escrow Agreement covering the licensing of the Company's software to Lee in the event of a default pursuant to the loan and security agreement. Interest for the year ended June 30, 2003 on these loans amounted to $15,393.

11. CONVERTIBLE LOAN DEBENTURES

On November 1, 2000, the Company entered into an Investment Agreement with Lee Enterprises

Incorporated ("Lee") whereby Lee provided funding of $1,500,000 in the form of a floating rate subordinated convertible debenture. The $1,500,000 subordinated convertible debenture consists of a series of six debentures of $250,000 that were received by the Company during the year ended June 30, 2001.

The Investment Agreement provides Lee the right to convert the floating rate subordinated convertible debenture into 6,902,429 common shares of the Company at a conversion price of $0.2173 per common share. If Lee does not convert the debenture into common shares, the Company will be required to repay the $1,500,000 loan on October 31, 2003. Each series of $250,000 subordinated convertible debenture bears interest at the Wall Street Journal rate less 1%. The weighted average effective rate for the year ended June 30, 2003 on these debentures was 3.40%. Interest for the year ended June 30, 2003 on these debentures amounted to $50,969.

On July 30, 2001, the Company and Lee entered into a First Amendment To Investment Agreement, which amended the Investment Agreement dated November 1, 2000 whereby Lee agreed to provide additional funding of $1,500,000 in the form of floating rate subordinated convertible debentures. The additional $1,500,000 subordinated convertible debentures were in the form of a series of twelve debentures (debentures "G-R") ranging in value from $50,000 to $310,000, which were funded during the period from August 10, 2001 to July 1, 2002. This resulted in a total investment by Lee of $3,000,000.

The first amendment to the Investment Agreement provides Lee the right to convert the second $1,500,000 floating rate subordinated convertible debenture into 8,522,727 common shares of the Company at a conversion price of $0.176. Should Lee convert both investments of $3,000,000 it would result in the Company issuing 15,425,156 common shares. If Lee does not convert the second debenture to common shares the Company will have to repay the $1,500,000 loan on October 31, 2003. Each Series "G-R" subordinated convertible debenture for the second investment of $1,500,000 bears interest at the Wall Street Journal rate less 1%.

In conjunction with the first amendment to the Investment Agreement dated July 30, 2001, the Company also amended the November 30, 2000 Loan and Security Agreement and the Collateral License Agreement and the Registration Rights Agreement to reflect the Series G-R debentures

On August 1, 2002, the Company and Lee entered into a Second Amendment To Investment Agreement, which amended the Investment Agreement dated November 1, 2000 whereby Lee agreed to provide additional funding of $300,000 in the form of floating rate subordinated convertible debentures. The additional $300,000 subordinated convertible debentures were in the form of a series of three debentures (debentures "S, T and U") ranging in value from $75,000 to $125,000, which were funded on August 1, 2002, September 1, 2002 and October 11, 2002 respectively. The weighted average effective rate for the year ended June 30, 2003 on these debenture series "G-U" was 3.39%. Interest for the year ended June 30, 2003 on these debentures amounted to $59,364.

11. CONVERTIBLE LOAN DEBENTURES (cont'd)

The second amendment to the Investment Agreement provides Lee the right to convert the $300,000 floating rate subordinated convertible debenture into 1,704,545 common shares of the Company at a conversion price of $0.176 per common share.

The second amendment to the Investment Agreement also contains certain affirmative and negative covenants that restrict the Company's activities. As of June 30, 2003, the Company is in compliance with the covenants in the Investment Agreement as amended. Interest due on the convertible debentures can be paid or converted into shares of the Company's common stock at fair market value on the date of conversion at the option of Lee.

On July 16, 2003 the Company and Lee entered into a Third Amendment To Investment Agreement, which amended the Investment Agreement dated November 1, 2000 whereby Lee agreed to provide additional funding of $100,000 in the form of floating rate subordinated convertible debenture. The additional $100,000 subordinated convertible debenture was in the form of a series "V" debenture, which was funded on July 16, 2003.

On August 14, 2003 the Company and Lee entered into a Fourth Amendment To Investment Agreement, which amended the Investment Agreement dated November 1, 2000 whereby Lee agreed to provide additional funding of $100,000 in the form of floating rate subordinated convertible debenture. The additional $100,000 subordinated convertible debenture was in the form of a series "W" debenture, which was funded on August 14, 2003.

12. DEMAND INSTALMENT LOAN

On January 10, 2003, the Company repaid its Demand instalment loan with the Canadian Imperial Bank of Canada from the proceeds of stockholder loans of two senior officers. *[Note 13[a]]*

13. RELATED PARTY TRANSACTIONS

[a] Stockholders' loans

In January 2003, the Company's chief executive officer and chief financial officer provided the Company $350,000 Cdn ($259,740 US) in the form of Stockholder loans.

In February 2003, the Company chief executive officer and chief financial officer provided the Company $59,000 Cdn ($43,785 US) in the form of Stockholder loans.

In May 2003, the Company chief executive officer and chief financial officer provided the Company $20,100 Cdn ($14,917 US) in the form of Stockholder loans.

[a] Stockholders' loans

At June 30, 2003 the Company has several unsecured stockholder loans denominated in Canadian dollars outstanding with the Company's chief executive officer and chief financial officer. The stockholders' loans, all of which are without stated terms of repayment unless otherwise stated, are payable on demand.

	Annual interest rate at June 30, 2003 %	Balance outstanding June 30 2003 $	June 30 2002 $
Loans payable bearing interest at 4.55% and repayable in equal monthly blended instalments of $1,450 through January 2028	**4.55**	**257,452**	—
Loans payable bearing interest at 4.55% and repayable in equal monthly blended instalments of $1,468 through January 2028	**4.55**	**250,462**	229,063
Loan payable bearing interest at Toronto Dominion Bank monthly TD Select Line rate	**7.75**	**36,334**	16,680
Loan payable bearing interest at the CIBC Visa monthly interest rate	**19.50**	**12,742**	13,344
Loan payable bearing interest at 4.5% per annum	**4.50**	**14,100**	7,876
Loan payable bearing interest at Canadian Imperial Bank of Canada monthly Line rate	**8.00**	**13,602**	—
Loan payable bearing interest at Canadian Imperial Bank of Canada monthly Line rate	**8.50**	**10,405**	—
Loan payable bearing interest at Canadian Imperial Bank of Canada monthly Line rate	**9.50**	**10,083**	—
Loan payable bearing interest at North Shore Credit Union monthly Line rate	**8.75**	**6,762**	—
Loan payable bearing interest at the Scotia McLeod monthly interest rate	—	—	5,873
		611,942	272,836

Interest incurred on the loans amounted to $24,884 for the year ended June 30, 2003 [2002 - $26,711].

13. RELATED PARTY TRANSACTIONS (cont'd.)

[b] Other

[i] On March 3, 2003, the Company granted 1,310,626 warrants to two of the Company's officers, as consideration for stockholders' loans totaling $350,000 Cdn ($259,740 US) that were made to the Company during the year ended June 30, 2003 [note 13[a]]. Each warrant is exercisable to purchase one common share of the Company at $0.18 per share through March 3, 2006 [note 16[c]]. The estimated fair value of these warrants at the date of issuance of $65,000 was recorded as an expense in the consolidated statement of loss for the year ended June 30, 2003. The Black Scholes options pricing model was used to value the warrants with the following assumptions: no dividend yield; risk-free interest rate of 5.0%; expected volatility of 140%; and an expected life of 3.0 years.

[ii] On June 16, 2003, the Company granted 782,187 warrants to two of the Company's officers, as consideration for stockholders' loans totaling $189,721 Cdn ($140,793 US) that were made to the Company during the year ended June 30, 2003 [note 13[a]]. Each warrant is exercisable to purchase one common share of the Company at $0.18 per share through June 16, 2006 [note 16[c]]. The estimated fair value of these warrants at the date of issuance of $15,644 was recorded as an expense in the consolidated statement of loss for the year ended June 30, 2003. The Black Scholes options pricing model was used to value the warrants with the following assumptions: no dividend yield; risk-free interest rate of 5.0%; expected volatility of 140%; and an expected life of 3.0 years.

14. OBLIGATIONS UNDER CAPITAL LEASES

The Company leases certain of its computer equipment under capital leases through fiscal year 2006. The future minimum lease payments required under capital leases as at June 30, 2003 are as follows:

	$
2004	83,202
2005	45,403
2006	6,902
Total minimum lease payments	135,507
Less: amounts representing interest	(16,922)
Present value of minimum lease payments	118,585
Less: current portion of obligations under capital leases	(70,812)
Long-term portion of obligations under capital leases	47,773

15. COMMITMENTS

The Company leases its premises and certain office equipment under operating leases expiring through fiscal year 2007. Future minimum lease commitments under these leases are as follows:

	Operating Leases $
2004	126,809
2005	114,558
2006	114,718
2007	95,598
Total future minimum lease payments	451,683

Rent expense for the year ended June 30, 2003 amounted to approximately $111,476 [2002 - $134,892].

16. SHARE CAPITAL

[a] Common stock

On July 25, 2001, the Company issued 100,000 common shares at $0.25 per share upon exercise of warrants. In lieu of cash payment, the exercise price was settled in payment of accounts payable of $25,000.

On December 12, 2001, the Company issued 160,000 common shares to a vendor for marketing services with a fair market value of $4,800.

On September 9, 2002, the Company issued 1,004,277 common shares to FP Canadian Newspapers Limited Partnership in connection with the acquisition of 10digit Communications *[Note 7]*.

On February 10, 2003, the Company issued the final tranche of 211,858 common shares to FP Canadian Newspapers Limited Partnership as part of the acquistion of 10digit Communications *[Note 7]*.

On April 17, 2003, the Company agreed to issue 198,587 common shares at $0.0637 per share to its board of directors for services with a fair market value of $12,650.

[b] Stock options

On August 25, 1999, and as amended on November 29, 2000 the Board of Directors approved the creation of the Corporate Stock Option Plan (“Plan”) pursuant to which the Company has reserved 3,000,000 [2000 - 2,000,000] shares of common stock. The term and vesting period of options are determined by the directors at the date of grant. The majority of the options granted to date are exercisable over a four year period and vest on a cumulative basis at 1/3 per year.

16. SHARE CAPITAL (cont'd.)

[b] Stock options

On November 29, 2001, the Company granted 75,000 stock options to a consultant for services rendered to the Company during the quarter ended December 31, 2001. Each stock option is exercisable into one common share of the Company at a price of $0.25 per share through November 30, 2004. The estimated fair value of these stock options at the date of issuance of $450 was recorded as an expense in the consolidated statement of operations for the quarter ended December 31, 2001. The Black Scholes option pricing model was used to value the warrants with the following assumptions: no dividend yield; risk-free interest rate of 5.0%; expected volatility of 153%; and an expected life of 3.0 years.

On December 19, 2002, at the Annual Shareholder Meeting the shareholders approved changes to the Corporate Stock Option Plan ("Plan") pursuant to which the Company has reserved a total of 4,000,000, [June 30, 2002 – 3,000,000] shares of common stock. The terms and vesting period of options are determined by the directors at the date of grant. The majority of the options granted to date are exercisable over a four-year period from the date the option was granted and vest on a cumulative basis at 1/3 per year.

Stock option transactions for the years ended June 30, 2003 and 2002 are summarized below:

	Shares available under option	Outstanding options	
		Shares	Weighted average exercise price
	#	#	$
Balance, June 30, 2001	1,100,000	1,900,000	0.25
Granted, November 29, 2001	(145,000)	145,000	0.25
June 28, 2002	(1,225,000)	1,225,000	0.25
Forfeited	380,000	(380,000)	0.25
Balance, June 30, 2002	110,000	2,890,000	0.25
Increased in reserved shares	1,000,000	—	—
Granted, January 30, 2003	(310,000)	310,000	0.25
Forfeited	50,000	(50,000)	0.25
Cancelled	200,000	(200,000)	0.25
Balance, June 30, 2003	1,050,000	2,950,000	0.25

The following table summarizes information about stock options that are outstanding at June 30, 2003:

	Options outstanding		Options exercisable	
Exercise price	Number outstanding at June 30, 2003	Weighted-average remaining contractual life	Number outstanding at June 30, 2003	Weighted-average exercise price
$	#		#	$
0.25	2,950,000	2.09	1,741,667	0.25

16. SHARE CAPITAL (cont'd.)

[c] Warrants

The following represents a summary of warrants outstanding at June 30, 2003:

	Outstanding warrants		
	Shares	Exercise price	
Grant Date	#	$	**Expiry date**
September 30, 1999	465,800	0.25	September 30, 2004
October 13, 1999	132,138	0.25	October 13, 2004
December 10, 1999	408,000	0.25	December 10, 2004
January 18, 2000	138,000	0.25	January 18, 2005
January 31, 2000	500,000	0.25	January 31, 2005
May 1, 2000	405,240	0.25	May 1, 2005
May 18, 2000	280,000	0.25	May 18, 2005
June 13, 2000	541,600	0.25	June 13, 2005
November 10, 2000	200,000	0.25	November 10, 2005
June 26, 2001	160,000	0.25	June 26, 2006
March 3, 2003	1,310,626	0.18	March 3, 2006
June 16, 2003	782,187	0.18	June 16, 2006
Balance, June 30, 2003	5,323,591		

Weighted average exercise price of all outstanding warrants at June 30, 2003 is $0.22.

Warrant transactions for the years ended June 30, 2003 and 2002 are summarized below:

	Outstanding warrants	
	Warrants	**Weighted average exercise price**
	#	$
Balance, June 30, 2001 and 2002	3,230,778	0.25
Granted, March 3, 2003	1,310,626	0.18
June 16, 2003	782,187	0.18
Balance, June 30, 2003	5,323,591	0.22

16. SHARE CAPITAL (cont'd.)

[c] Warrants (cont'd.)

On July 14, 2001, 45,260 warrants with an exercise price of $0.25 expired unexercised.

On September 29, 2001, the Company extended the expiry dates of all outstanding warrants issued in connection with private placements and loan guarantees by one year.

On June 28, 2002, the Company extended the expiry dates of all outstanding warrants issued by an additional two years.

[d] Loss per common share

The following table sets forth the computation of basic and diluted loss per share:

	2003 $	**2002** $
Net loss for the year	**(1,124,582)**	(1,829,444)
Net loss attributable to common shareholders	**(1,124,582)**	(1,829,444)
Weighted average number of common shares outstanding	**24,194,083**	23,222,231
Basic and diluted loss per common share	**(0.05)**	(0.08)

For the years ended June 30, 2003 and 2002, all of the Company's common shares issuable upon the exercise of 2,950,000 (2002 - 2,890,000) stock options and 5,323,591 (2002 - 4,541,404) warrants were excluded from the determination of diluted loss per common share as their effect would be anti-dilutive.

[e] Authorized share capital

On November 29, 2001, the shareholders approved in the Annual General Meeting an increase in the Company's authorized share capital from 50,000,000 no par value common shares to 100,000,000 no par value common shares.

17. INCOME TAXES

The Company is subject to United States Federal Taxes at an approximate rate of 34%. It is also subject to Canadian Federal and British Columbia provincial taxes of approximately 45%. No current provision or benefit for income taxes has been recorded for the years ended June 30, 2003 or 2002 as the Company has incurred operating losses and has no carryback potential.

The Company's deferred income tax recovery for the year ended June 30 comprises:

	2003 $	**2002** $
United States	**—**	(93,100)
Canada	**—**	—
	—	(93,100)

The reconciliation of income tax attributable to continuing operations computed at the U.S. federal statutory tax rates to income tax expense for the years ended June 30 is:

	2003 $	**2002** $
Tax at U.S. statutory rates	**(360,000)**	(653,000)
Higher effective income taxes of other country	**(46,000)**	(168,000)
Deferred tax assets not recognized for accounting purposes	**80,000**	52,000
Tax losses not recognized for accounting purposes	**209,000**	640,000
Other	**117,000**	35,900
Income tax recovery	**—**	(93,100)

17. INCOME TAXES (cont'd.)

Net deferred tax assets (liabilities) consist of the following at June 30:

	2003 $	**2002** $
Deferred tax assets		
Loss carryforwards	**3,060,000**	2,800,000
Tax values in excess of book value	**201,000**	44,000
Valuation allowance for future tax assets	**(3,261,000)**	(2,844,000)
Net deferred tax assets	**—**	—

The tax losses expire as follows:

	U.S. $	**Canadian** $
2004	**—**	4,000
2005	**—**	180,000
2006	**—**	1,180,000
2007	**—**	1,610,000
2008	**—**	1,790,000
2009	**—**	1,410,000
2010	**—**	414,000
2019	78,000	**—**
2020	5,000	**—**
2021	13,000	**—**
2022	67,000	**—**
	163,000	6,588,000

18. SEGMENT INFORMATION

Predominantly all of the Company's assets and employees are located in Canada for the years presented. The following table represents total revenues based on the location of the customer:

	2003 $	**2002** $
U.S.A.	**984,878**	363,509
Canada	**188,603**	51,021
Total revenues	**1,173,481**	414,530

19. COMPARATIVE FIGURES

Certain comparative figures have been reclassified from statements previously presented to conform to the presentation adopted in the current year.

20. SUBSEQUENT EVENTS

On July 16, 2003, the Company entered into the Third Amendment to the Investment Agreement whereby Lee advanced an additional $100,000 Series "V " debenture and on August 14, 2003, the Company entered into the Fourth Amendment to the Investment Agreement whereby Lee advanced an additional $100,000 Series "W" debenture.