Consolidated Financial Statements

CityXpress Corp.

(Expressed in U.S. dollars)
June 30, 2004 and 2003

Grant Thornton

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, 2004 and 2003, and the related consolidated statements of operations, stockholders' equity (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, 2004 and 2003 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 accumulated losses from operations and is currently dependent on its ability to raise capital from shareholders or other sources to sustain operations. These factors raise some 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 17, 2004

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)

	2004 $	2003 $
ASSETS *[note 9]*		
Current		
Cash and cash equivalents	**1,329,248**	12,308
Accounts receivable, net of allowance for doubtful accounts of $nil in 2004 and 2003 *[note 4]*	**334,157**	94,169
Other receivables	**4,936**	7,132
Prepaid expenses and other	**21,424**	26,603
Total current assets	**1,689,765**	140,212
Property and equipment *[note 5]*	**141,389**	124,465
Software development costs *[note 6]*	**207,896**	171,579
Intangible assets *[note 7]*	**28,512**	53,492
Total assets	**2,067,562**	489,748
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current		
Accounts payable *[note 8]*	**173,526**	291,423
Accrued liabilities *[note 8]*	**198,178**	421,423
Deferred revenue	**532,349**	250,763
Revolving loan *[note 9]*	**—**	66,790
Loans payable *[note 10]*	**—**	350,000
Convertible loan debentures *[note 11]*	**—**	3,300,000
Stockholders' loans *[note 12]*	**559,829**	611,942
Current portion of obligations under capital leases *[note 13]*	**58,173**	70,812
Total current liabilities	**1,522,055**	5,363,153
Obligations under capital leases *[note 13]*	**46,111**	47,773
Total liabilities	**1,568,166**	5,410,926
Commitments *[note 14]*		
Stockholders' equity (deficiency)		
Share capital *[note 15]*		
Common stock - $0.001 par value		
Authorized shares: 150,000,000		
Issued and outstanding: 85,992,502 at June 30, 2004 and 24,520,033 at June 30, 2003	**85,993**	24,520
Common stock to be issued – nil at June 30, 2004 and 198,587 at June 30, 2003	**—**	12,650
Additional paid in capital	**12,050,698**	5,984,090
Accumulated other comprehensive income	**19,625**	19,625
Deficit	**(11,656,920)**	(10,962,063)
Total stockholders' equity (deficiency)	**499,396**	(4,921,178)
Total liabilities and stockholders' equity (deficiency)	**2,067,562**	489,748

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)

	2004 $	2003 $
Revenue *[note 4]*		
Auctions	**2,395,089**	784,963
Special Sections	**267,837**	388,518
Total revenues	**2,662,926**	1,173,481
Cost of sales (including amortization of product development costs of $124,204, 2003 - $81,793)	**1,292,137**	542,334
Gross profit	**1,370,789**	631,147
Operating expenses		
Sales and marketing	**903,197**	573,675
Software development and technology	**458,341**	364,535
Finance and administration	**562,374**	448,728
	1,923,912	1,386,938
Operating loss	**(553,123)**	(755,791)
Other income (expense)		
Interest expense	**(110,420)**	(253,905)
Interest and miscellaneous income	**299**	63
Gain on disposal of property and equipment	**250**	—
Foreign exchange loss	**(31,863)**	(114,949)
Total other expense	**(141,734)**	(368,791)
Loss before income taxes	**(694,857)**	(1,124,582)
Deferred income tax recovery *[note 16]*	—	—
Net loss and comprehensive loss for the year	**(694,857)**	(1,124,582)
Net loss per common share *[note 15[d]]*		
Basic and diluted	**(0.02)**	(0.05)
Weighted average number of common shares *[note 15[d]]*		
Basic and diluted	**28,892,850**	24,194,083

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, 2003								
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 15[a]]*	1,216,135	—	1,216	—	60,141	—	—	61,357
Shares to be issued for services received in 2003 *[note 15(a)]*	—	107,928	—	6,875	—	—	—	6,875
Shares to be issued for cancellation of stock options *[note 15[a]]*	—	90,659	—	5,775	—	—	—	5,775
Stock based compensation	—	—	—	—	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)
Shares issued for services received in 2003	107,928	(107,928)	108	(6,875)	6,767	—	—	—
Shares issued for cancellation of stock options	90,659	(90,659)	91	(5,775)	5,684	—	—	—
Shares issued for convertible loan debentures *[notes [11] and 15[a]]*	18,266,065	—	18,266	—	3,481,734	—	—	3,500,000
Shares issued for loans payable and interest accrued *[notes [10] and 15[a]]*	12,370,876	—	12,371	—	680,398	—	—	692,769
Shares issued for Knight Ridder investment *[note 15(a)]*	30,636,941	—	30,637	—	1,969,363	—	—	2,000,000
Legal fees	—	—	—	—	(77,338)	—	—	(77,338)
Net loss for the year	—	—	—	—	—	—	(694,857)	(694,857)
Balance at June 30, 2004	85,992,502	—	85,993	—	12,050,698	19,625	(11,656,920)	499,396

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)

	2004 $	2003 $
OPERATING ACTIVITIES		
Net loss for the year	**(694,857)**	(1,124,582)
Adjustments to reconcile net loss to net cash used in operating activities:		
Amortization	**24,980**	21,450
Depreciation	**234,223**	178,694
Shares to be issued for services rendered	**—**	12,650
Stock based compensation	**—**	80,644
Deferred revenue	**281,586**	239,497
Changes in operating assets and liabilities:		
Accounts receivable	**(239,988)**	(91,078)
Other receivables	**2,196**	(2,844)
Prepaid expenses and other	**5,179**	(10,274)
Accounts payable	**(117,897)**	82,223
Accrued liabilities	**119,524**	177,227
Net cash used in operating activities	**(385,054)**	(436,393)
INVESTING ACTIVITIES		
Software development costs	**(181,886)**	(121,694)
Purchase of property and equipment	**(35,986)**	(12,292)
10digit Communications acquisition costs *[note 7]*	**—**	(13,585)
Net cash used in investing activities	**(217,872)**	(147,571)
FINANCING ACTIVITIES		
Proceeds from issuance of common shares (net of share issue costs)	**1,922,662**	—
Proceeds from convertible loan debentures	**200,000**	300,000
Repayments under capital leases	**(83,893)**	(39,688)
Repayment of revolving loan	**(66,790)**	—
Repayment of stockholders' loans	**(52,113)**	(9,856)
Proceeds from stockholders' loans	**—**	348,962
Repayment of demand instalment loan	**—**	(152,910)
Proceeds from revolving loan	**—**	66,790
Net cash provided by financing activities	**1,919,866**	513,298
Net increase (decrease) in cash and cash equivalents during the year	**1,316,940**	(70,666)
Cash and cash equivalents, beginning of year	**12,308**	82,974
Cash and cash equivalents, end of year	**1,329,248**	12,308
Non cash financing and investing transactions not included in cash flows:		
Capital assets acquired through the assumption of capital leases	**69,592**	88,886
Shares issued to acquire 10digit Communications	**—**	61,357
Conversion of convertible loan debentures to common stock	**3,500,000**	—
Conversion of demand installment loan to common stock	**350,000**	—
Conversion of accrued interest on loans payable to common stock	**342,769**	—
Supplemental disclosure		
Interest paid	**80,927**	47,535

See accompanying notes

CityXpress Corp.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2004 and 2003 (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 and European markets.

The consolidated financial statements for the year ended June 30, 2004 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 $694,857 for the year ended June 30, 2004 and has an accumulated deficit of $11,656,920 at June 30, 2004. These factors raise some 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 or to obtain additional capital. Management expects to generate higher revenues over the 2005 fiscal year. If the Company is unable to increase revenues or obtain additional capital, 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.

Software development costs

Cost for the development of new software and substantial enhancements to existing software are expensed as incurred until technological possibility has been established, at which time any additional development costs are capitalized in accordance with Statement of Financial Accounting Standards ("SFAS") No. 86 "*Computer Software to be Sold, Leased or Otherwise Marketed*".

Product development costs are amortized on a straight-line basis 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 are being amortized on a straight-line basis over their useful life, which is 36 months.

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

2005	$24,982
2006	$3,530
2007	$Nil
2008	$Nil
2009	$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 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 years ended June 30 was as follows:

	Options #	Weighted average fair value $
2004		
Exercise price:		
Greater than fair market value	1,804,040	0.02
	1,804,040	0.02
2003		
Exercise price:		
Greater than fair market value	310,000	0.10
	310,000	0.10

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 3% [2003- 5%]; dividend yields of nil; volatility factors of the expected market price of the Company's common stock of 269% [2003– 140%] and a weighted average expected life of the option of 10.00 years [2003 – 4.00 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:

		2004 $	2003 $
Net loss	As reported	**(694,857)**	(1,124,582)
SFAS 123 compensation expense	Pro forma	—	(31,000)
Pro forma net loss attributable to common stockholders	Pro forma	**(694,857)**	(1,155,582)
Weighted average number of common shares outstanding		**28,892,850**	24,194,083
Pro forma net loss per common share:			
Basic and diluted	Pro forma	**(0.02)**	(0.05)

For the year ended June 30, 2004, all options issued were to replace warrants that were cancelled during the year (Note 15(c)). Variable accounting has been applied to these options using the fair value method in accordance with SFAS 123. As such, there is no proforma disclosure required for these options.

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 fees, 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.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd.)

Advertising costs

Advertising costs are expensed as incurred and amounted to $56,600 in the year ended June 30, 2004 [2003 - $53,471].

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, 2004 and 2003, all outstanding options and warrants were anti-dilutive.

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 the range of management's expectations.

For the year ended June 30, 2004, the Company has two (2003-one) customers sales to each of whom exceeded 10% of the total sales. These two customers account for 29% (2003- 26%) of the Company's total revenues. At June 30, 2004, approximately 24% of the Company's accounts receivable balance was due from these two customer (2003 – 19%).

These two customers are also significant shareholders of the company (see Note 12 (c)).

5. PROPERTY AND EQUIPMENT

	2004		2003	
	Cost $	**Accumulated depreciation** $	**Cost** $	**Accumulated depreciation** $
Computer equipment and software	**207,893**	**171,320**	175,383	156,003
Computer equipment under capital leases	**258,433**	**162,944**	184,966	91,163
Office furniture and equipment	**25,565**	**16,761**	22,802	12,170
Leasehold improvements	**8,189**	**7,666**	8,189	7,539
	500,080	**358,691**	391,340	266,875
Net book value	**141,389**		124,465	

6. SOFTWARE DEVELOPMENT COSTS

	2004 $	**2003** $
Cost	**524,788**	342,902
Accumulated depreciation	**316,892**	171,323
	207,896	171,579

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, the following proforma results of operations have been estimated:

	Year Ended June 30 2003 (Unaudited) $
Revenue	1,173,481
Net Loss	(1,124,582)
Net Loss per share (Basic and Diluted)	(0.05)

	2004 $	**2003** $
Intangible assets	**74,942**	74,942
Accumulated amortization	**46,430**	21,450
	28,512	53,492

8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	2004 $	2003 $
Trade accounts payable	**173,526**	291,423
Accrued interest	**1,663**	314,462
Accrued vacation	**73,617**	52,317
Other accrued liabilities	**122,898**	54,644
Total Accrued liabilities	**198,178**	421,423

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 $377,000 Cdn ($281,343 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, 2004 on this loan amounted to $15,272. On June 7, 2004, the Company repaid the remaining balance of the revolving loan.

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, 2004
August 17, 2000	125,000	October 31, 2003	4.00
August 28, 2000	125,000	October 31, 2003	4.00
September 19, 2000	40,000	October 31, 2003	4.00
July 12, 2001	60,000	October 31, 2003	4.00
	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, 2004 on these loans amounted to $3,529. On June 14, 2004, the Company converted Lee's $350,000 loan to 6,250,000 common shares at $0.056 per share.

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 consisted of a series of six debentures (debentures "A-F") 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 at a conversion price of $0.2173 per common share. If Lee does not convert the debenture into common shares, the Company was required to repay the $1,500,000 loan on October 31, 2003. Each series of $250,000 subordinated convertible debenture bore interest at the Wall Street Journal rate less 1%.

On July 30, 2001, the Company and Lee entered into a First Amendment To Investment Agreement ("The July 30, 2001 Amendment"), 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 July 30, 2001 Amendment provided Lee the right to convert the second $1,500,000 floating rate subordinated convertible debenture into 8,522,727 common shares at a conversion price of $0.176. If Lee converted both investments of $3,000,000 it would result in the Company issuing 15,425,156 common shares. If Lee did not convert the second debenture to common shares, the Company would have had 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 bore interest at the Wall Street Journal rate less 1%.

On August 1, 2002, the Company and Lee entered into a Second Amendment To Investment Agreement ("The August 1, 2002 Amendment"), which amended the Investment Agreement dated November 1, 2000 whereby Lee provided 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 August 1, 2002 Amendment provided 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.

11. CONVERTIBLE LOAN DEBENTURES (cont'd)

The August 1, 2002 Amendment also contained certain affirmative and negative covenants that restricted the Company's activities. Interest due on the convertible debentures could be paid or converted into 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 a 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 a 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.

The weighted average effective rate for the year ended June 30, 2004 on all these debenture series "A-W" was 3.00% (2003: 3.40%). Interest for the year ended June 30, 2004 on these debentures amounted to $25,964 (2003: $110,333).

On May 14, 2004, the Company converted Lee's $3,500,000 convertible debenture to 18,266,065 common shares at an average conversion price of $0.1916 per share.

12. 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.

In July 2003, the Company chief executive officer and chief financial officer provided the Company $100,000 Cdn ($74,626 US) in the form of Stockholder loans.

In June 2004, the Company paid $113,672 Cdn ($84,830 US) toward the Company's outstanding loans from its chief executive officer and chief financial officer in addition to monthly payments totaling $52,918 Cdn ($41,909 US) during the year.

12. RELATED PARTY TRANSACTIONS (cont'd.)

[a] Stockholders' loans (cont'd)

At June 30, 2004 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, 2004 %	Balance outstanding June 30 2004 $	June 30 2003 $
Loans payable bearing interest at 4.55% and repayable in equal monthly blended instalments of $1,450 through January 2028	**4.55**	**251,550**	257,452
Loans payable bearing interest at 4.55% and repayable in equal monthly blended instalments of $1,468 through January 2028	**4.55**	**238,361**	250,462
Loans payable bearing interest at 4.55% and repayable in equal monthly blended instalments of $1,468 through January 2028	**5.10**	**69,918**	—
Loan payable bearing interest at Toronto Dominion Bank monthly TD Select Line rate	**7.75**	—	36,334
Loan payable bearing interest at the CIBC Visa monthly interest rate	**19.50**	—	12,742
Loan payable bearing interest at 4.5% per annum	**4.50**	—	14,100
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
		559,829	611,942

Interest incurred on the loans amounted to $37,261 for the year ended June 30, 2004 [2003 - $24,884].

12. RELATED PARTY TRANSACTIONS (cont'd.)

[b] Warrants

[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 12[a]]. Each warrant was exercisable to purchase one common share of the Company at $0.18 per share through March 3, 2006 [note 15[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. During fiscal 2004, these warrants were cancelled and replaced with options to purchase the Company's common shares at $0.0653 per share for 10 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 12[a]]. Each warrant was exercisable to purchase one common share of the Company at $0.18 per share through June 16, 2006 [note 15[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. During fiscal 2004, these warrants were cancelled and replaced with options to purchase the Company's common shares at $0.0653 per share for 10 years.

[c] Other

The following table summarizes sales made during the year and receivables balances at the year end with the two significant shareholders:

	2004 $	**2003** $
Lee Enterprises, a 35.63% shareholder		
Sales	**350,563**	280,081
Accounts receivable balances	**3,713**	1,708
Knight Ridder Investment Company, a 35.63% shareholder		
Sales	**409,421**	27,920
Accounts receivable balances	**76,449**	16,310

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

13. OBLIGATIONS UNDER CAPITAL LEASES

The Company leases certain of its computer equipment under capital leases through fiscal year 2008. The future minimum lease payments required under capital leases as at June 30, 2004 are as follows:

	$
2005	75,181
2006	36,617
2007	19,501
2008	546
Total minimum lease payments	131,845
Less: amounts representing interest	(27,561)
Present value of minimum lease payments	104,284
Less: current portion of obligations under capital leases	(58,173)
Long-term portion of obligations under capital leases	46,111

14. 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 $
2005	117,669
2006	110,979
2007	95,598
Total future minimum lease payments	324,246

Rent expense for the year ended June 30, 2004 amounted to approximately $123,345 [2003 - $111,476].

15. SHARE CAPITAL

[a] Common stock

In fiscal 2003, the Company issued 1,216,135 common shares to FP Canadian Newspapers Limited Partnership in connection with the acquisition of 10digit Communications *[Note 7]*.

On April 17, 2003, the Company agreed to issue 107,928 common shares at $0.0637 per share to its board of directors for services with a fair market value of $6,875. On the same date, the Company also agreed to issue 90,659 common shares at $0.0637 per share to certain directors for cancellation of stock options with a fair market value of $5,775. These shares were issued on October 24, 2003.

On May 14, 2004, the Company issued 18,266,065 common shares at $0.1916 per share to Lee Enterprises for conversion of its $3,500,000 loan debenture. (Note 11)

15. SHARE CAPITAL (cont'd)

[a] Common stock (cont'd)

On June 14, 2004, the Company issued 6,250,000 common shares at $0.056 per share to Lee Enterprises for conversion of its $350,000 loans payable. (Note 10)

On June 14, 2004, the Company issued 6,120,876 common shares at $0.056 per share to Lee Enterprises for conversion of $342,769 interest accrued on Lee's $3,500,000 convertible debenture and $350,000 loan payable.

On June 14, 2004, the Company issued 30,636,941 common shares at $0.0652 per share to Knight Ridder for its $2,000,000 equity investment.

[b] Stock options

On August 25, 1999, and as amended on November 29, 2000, December 19, 2002 and May 28, 2004 the Board of Directors approved the creation of the Corporate Stock Option Plan ("Plan") pursuant to which the Company has reserved 10,500,000 [June 30, 2003 - 4,000,000] shares of common stock. The term and vesting period of options are determined by the directors at the date of grant.

On May 28, 2004, the Company cancelled 2,775,000 outstanding stock options issued to employees and directors.

On June 1, 2004, the Company granted 1,779,040 stock options to three directors pursuant to the Investment Agreement with Knight Ridder and approval by the shareholders at the Annual Shareholder Meeting. These stock options vest immediately and are exercisable for ten years with an exercise price of $0.0653 per share.

Stock option transactions for the years ended June 30, 2004 and 2003 are summarized below:

	Shares available under option	Outstanding options	
		Shares	Weighted average exercise price
	#	#	$
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
Increase in reserved shares	6,500,000	—	—
Granted, July 17, 2003	(25,000)	25,000	0.25
Granted, June 1, 2004	(1,779,040)	1,779,040	0.0653
Forfeited	125,000	(125,000)	0.25
Cancelled	2,775,000	(2,775,000)	0.25
Balance, June 30, 2004	8,645,960	1,854,040	0.0728

15. SHARE CAPITAL (cont'd)

[b] Stock options (cont'd)

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, 2004 #	Weighted-average remaining contractual life	Number outstanding at June 30, 2004 #	Weighted-average exercise price $
0.25	75,000	0.42	75,000	0.25
0.0653	1,779,040	9.92	1,779,040	0.0653
0.0728	1,854,040	9.54	1,854,040	0.0728

[c] Warrants

The following represents a summary of warrants outstanding at June 30, 2004:

	Outstanding warrants		
	Shares	Exercise price	
Grant Date	#	$	Expiry date
October 13, 1999	132,138	0.25	October 13, 2004
January 18, 2000	138,000	0.25	January 18, 2005
May 18, 2000	280,000	0.25	May 18, 2005
Balance, June 30, 2004	550,138		

Warrant transactions for the years ended June 30, 2004 and 2003 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
Cancelled, June 14, 2004	(4,773,453)	0.22
Balance, June 30, 2004	550,138	0.25

On June 14, 2004, the Company cancelled 4,773,453 outstanding warrants and issued 1,779,040 replacement stock options pursuant to the Investment Agreement with Knight Ridder and approval by the shareholders at the Annual Shareholder Meeting. These stock options vest immediately and are exercisable for ten years with an exercise price of $0.0653 per share.

15. SHARE CAPITAL (cont'd.)

[d] Loss per common share

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

	2004 $	**2003** $
Net loss for the year	**(694,857)**	(1,124,582)
Net loss attributable to common shareholders	**(694,857)**	(1,124,582)
Weighted average number of common shares outstanding	**28,892,850**	24,194,083
Basic and diluted loss per common share	**(0.02)**	(0.05)

For the years ended June 30, 2004 and 2003, all of the Company's common shares issuable upon the exercise of 1,854,040 (2003 - 2,950,000) stock options and 550,138 (2003 – 5,323,591) warrants were excluded from the determination of diluted loss per common share as their effect would be anti-dilutive.

[e] Authorized share capital

On May 28, 2004, the shareholders approved in the Annual General Meeting an increase in the Company's authorized share capital from 100,000,000 common shares with a par value of $0.001 per share to 150,000,000 common shares with a par value of $0.001 per share.

16. 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 37%. No current provision or benefit for income taxes has been recorded for the years ended June 30, 2004 or 2003 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:

	2004 $	**2003** $
United States	—	—
Canada	—	—
	—	—

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:

	2004 $	**2003** $
Tax at U.S. statutory rates	**(236,000)**	(360,000)
Higher effective income taxes of other country	**(17,000)**	(46,000)
Deferred tax assets not recognized for accounting purposes	**56,000**	80,000
Tax losses not recognized for accounting purposes	**132,000**	209,000
Other	**65,000**	117,000
Income tax recovery	—	—

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

	2004 $	**2003** $
Deferred tax assets		
Loss carryforwards	**2,600,000**	3,060,000
Tax values in excess of book value	**220,000**	201,000
Valuation allowance for future tax assets	**(2,820,000)**	(3,261,000)
Net deferred tax assets	—	—

16. INCOME TAXES (cont'd.)

The tax losses expire as follows:

	U.S.	Canadian
	$	$
2005	—	181,000
2006	—	1,152,000
2007	—	1,579,000
2008	—	1,703,000
2009	—	1,412,000
2010	—	415,000
2011	—	357,000
2019	78,000	—
2020	5,000	—
2021	13,000	—
2022	140,000	—
	236,000	6,799,000

17. 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:

	2004	2003
	$	$
U.S.A.	**2,329,910**	984,878
Canada	**304,199**	188,603
Europe	**28,817**	—
Total revenues	**2,662,926**	1,173,481

18. COMPARATIVE FIGURES

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