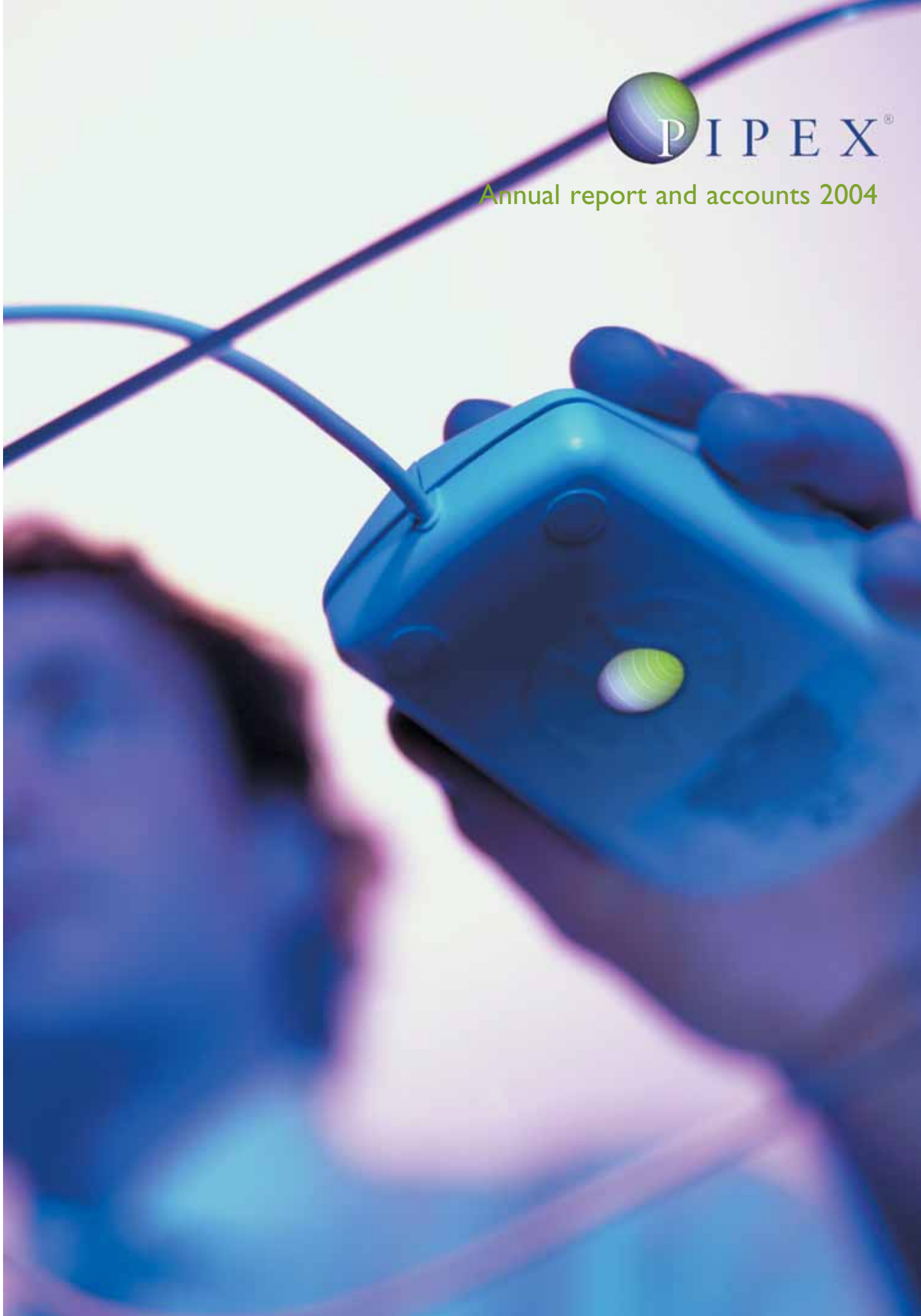




Annual report and accounts 2004



## GLOSSARY OF TERMS

**Backbone network** A major transmission path that can carry a very high volume of traffic. It ensures that all smaller networks that are connected to the backbone are also connected to each other.

**Bandwidth** A measurement of the quantity of information that can be transmitted via communications channels such as fibre. This is measured in megabits per second.

**Broadband** Network technology that allows the transmission of large amounts of data.

**Broadband internet** Technology that enables faster internet access, and as a result allows services such as interactive digital TV, video conferencing and video e-mail.

**Data** Information sent across communications networks from computer to computer.

**DSL (Digital subscriber line)** DSL is a technology that transforms ordinary phone lines (also known as 'twisted copper pairs') into high-speed digital lines. ADSL uses digital coding techniques to squeeze up to 99 per cent more capacity out of a phone line without interfering with regular telephone service. Can be used to transmit voice and data simultaneously and provide a continuous connection for data services.

**Intelligent network (IN)** A network that allows the fast and flexible introduction of new services and customisation capabilities for users of that network.

**IP (Internet protocol)** A standard specification for transmitting voice and data over the internet.

**ISP (Internet service provider)** A company which provides users with access to the Internet.

**Leased line** A reliable, dedicated network connection offered at various speeds depending on the customer's requirements.

**Mbps** Megabits per second – a measure of bandwidth.

**POP (Point of presence)** A point of presence is a physical location where the end user connects to an ISP network to gain Internet connectivity.

### Broadband services



### Hosting services



### Network services



PIPEX IS ONE OF THE UK'S LEADING TELECOM NETWORK OPERATORS AND PROVIDER OF BROADBAND SOLUTIONS COMBINING THE BEST INFRASTRUCTURE, SERVICES, SUPPORT AND PEOPLE. AS A HIGHLY RESPECTED TIER ONE INTERNET SERVICE PROVIDER (ISP), PIPEX PROVIDES BOTH VOICE AND DATA CONNECTIVITY SOLUTIONS, HOSTING AND SECURITY SERVICES.

**% of revenue**

Broadband is the Internet access method of choice for the Residential and SME market place. As the 5th largest supplier of DSL services in the UK, PIPEX bundles additional services, including voice and security, increasing the value-added appeal of the access services.

54%

Hosting services encompass shared hosting, primarily for SMEs to present their business websites. Larger customers are supported via dedicated servers and co-location. A key element of all hosting services is the delivery of domain names and security.

16%

Network services covers all aspects of network support for medium and large businesses involving Virtual Private Networks, dedicated access, voice, security and complex hosting solutions. PIPEX supplies tailored, managed solutions integrating any or all of these.

30%

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“WE FELT THAT THE SOLUTION PIPEX SUGGESTED MET ALL OF OUR CORPORATE CRITERIA AND THAT THE COMPANY COULD ALSO OFFER US A SOUND WORKING PARTNERSHIP”  
TESCO

### Overview

I am pleased to report that during 2004 PIPEX has grown significantly and is reporting its first full year positive EBITDA (pre-integration costs and UITF 17 charges) of £13.6m (FY 2003: equivalent loss of £3.1m) and profit before tax, amortisation, business integration costs and UITF 17 charges of £6.2m (FY 2003: equivalent loss of £7.2m). Revenues increased threefold, to £102.3m, gross margins continue to improve to 47.4% against 43.5% in FY 2003 and over £6.0m of annualised cost savings have been realised during the year. In addition, PIPEX was free cash flow positive in 2004.

Following a sustained programme of acquisition and integration, PIPEX is now a leading telecoms network operator and provider of broadband, hosting and network services. We ended the year with 420,000 customers and a clear focus on the high growth areas of 'new wave' IP revenues, in broadband, hosting and network services.

In 2004 PIPEX improved its position in these high growth markets with the acquisitions of Host Europe plc and Nildram. Host Europe plc was acquired in April 2004 for a net cash cost of £26.5m and strengthens our offering in the shared hosting and domain registration business. It brought with it 127,000 hosting

customers and 732,000 domain names to the group. Nildram, acquired in August 2004 for £13.0m before expenses, is predominantly a broadband service provider, servicing 35,000 customers across the residential, SME and large corporate sectors.

The group's focus on the optimisation of its infrastructure continues, with particular emphasis on back office systems. The network itself also continues to be enhanced and developed, and we expect its total integration to be completed in the second half of 2005.

During the year we have sought to improve our position in the marketplace by overhauling our sales channel and customer web interfaces. As a result, there has been a complete transformation during 2004 in the way PIPEX sells its products: 70% of sales are now generated via the group's websites, up from 25% in 2003. This, together with staff productivity improvement, has led to average annual revenue per employee increasing 47% to £178,000 since year end 2003. There has also been a resultant improvement in operating expenses (pre-amortisation, depreciation, integration costs and UITF 17 charges), as a percentage of revenue, having fallen from 54% to 35%.

### Broadband service

PIPEX is now the 5th largest supplier of broadband in the UK and ended 2004 with 192,000 customers (versus 93,000 at the end of 2003). This growth has been achieved while also increasing ARPU per customer from £24 to £25 per month. We have maintained a strong customer mix, with business customers comprising 20% of the total.

The building blocks for bundling services such as voice, security and hosting to our broadband customers have been put in place during 2004, and this is our key area of focus for the year ahead for this division, creating customer loyalty and driving an increase in ARPU. Voice has been launched on our Nildram product and we are encouraged by initial signs, with 20% of new customers adding voice to their broadband service.

### Hosting services

PIPEX is a leading provider of shared and dedicated hosting as well as the largest provider of domain names in the UK, achieving strong organic growth and ending the year with 935,000 registered domain names and 154,000 hosting services customers.

Our data centres ended 2004 with an average of over 60% occupancy. During the year we enhanced network resilience between the



#### Summary

- Revenues increased three-fold
- Gross margins continue to improve
- Free cash flow positive in 2004
- Acquisition of Host Europe and Nildram
- £20.0m of annualised cost savings from acquisitions over two years
- Strengthened management team
- 70% of sales generated via group's websites

## PROVEN PERFORMANCE

data centres and our customers. We continue to modify and update the product set and recently launched a Microsoft shared hosting solution to our customers.

Our hosting centre in Germany benefited from extremely strong growth in 2004 and the data centre ended the year at 80% capacity. We see potential for further strong growth in this territory in 2005, and plans are in place for strengthening our German presence with a second data centre.

#### Network services

Since the four acquisitions made during 2002 and 2003, the network services division has been focused on integration, both at an infrastructure and product level. The companies are now fully operationally integrated and selling a broad range of products, including leased lines, MPLS, VPN, gigabit ethernet, security, hosting solutions and wireless products. For the most part, these are carried on our Fibernet backbone, which has over twenty years remaining on our IRU. These efforts have resulted in the division starting to deliver organic growth during 2004, a trend which has continued strongly into 2005. At the year end, the division had 2,000 corporate customers, and we are encouraged by a number of significant contract wins at the beginning of 2005.

#### Operational performance

Turnover increased in the year to £102.3m, with £78.4m coming from existing operations (up from £35.2m in 2003), and £23.9m contributed by our 2004 acquisitions. Gross margin also grew by 3.9 percentage points to 47.4%, reflecting our strategy to develop a portfolio of services in growing markets without being over-exposed in any one area. In 2004, the acquisition of Host Europe added high margin Hosting services to this

portfolio, lifting our overall margin. In my statement last year, I reported that the Company had become EBITDA positive on a month-by-month basis by the 2003 year end. In 2004 we report significant progress in this area, with EBITDA pre-integration costs and UITF 17 charges of £13.6m. PIPEX was also free cash flow positive in 2004, providing a solid platform for our further development.

#### Management team

The senior management team has been strengthened during 2004. Maria Cappella, with eighteen years of telecoms and IT experience, joined us as General Manager of Sales and Marketing, while Sean Stephenson, founder of Nildram, has joined the senior management team. John Whitty, with twenty years of telecoms experience, is our CTO, while Dominic Crolla heads up the Broadband operation and Rick Flood, ex-COO of Host Europe, is Head of Hosting services. PIPEX now has an extremely strong and experienced team lead by our CEO Mike Read.

#### Financing

In the year, the Company raised £33.0m (before expenses) from the issue of new shares to finance the Host Europe acquisition. We also increased our debt facility with Bank of Scotland by £13.0m to fund the purchase of Nildram.

#### Outlook

The 3.6 – 4.2 GHz national wireless licence which PIPEX owns remains an extremely important asset to the group. This frequency falls within the new WIMAX standard and to this end PIPEX and a partner will be trialling this in Q3 2005.

As more people subscribe to Broadband Internet access, the amount of traffic and data that is being created is increasing rapidly. This has now reached a point where our

corporate customers, providing services over the web, are upgrading their network requirements, and where more new companies are seeing the benefits of having their own presence on the Internet. Broadband in the home is also creating a demand among consumers for bundled IP services, including voice, hosting and, eventually, content.

With these positive market conditions and the strong initial trading in 2005 in mind, we believe PIPEX is set to enjoy strong growth for the year, across all three divisions.

**Peter Dubens** Chairman

8 April 2005



“WE ARE DELIGHTED WITH EVERY ASPECT OF THE CONNECTION AND SERVICE THAT PIPEX PROVIDE”

COVENTRY UNIVERSITY ENTERPRISES

Welcome to our 2004 Annual Report. As predicted last year, 2004 has seen a number of consolidations in the telecommunications market, and PIPEX Communications is no exception. We have added Nildram (the broadband services provider), Trinité (a managed network/application services provider), and Host Europe plc (one of Europe's leading Internet hosting companies) to our group.

The acquisitions and strong growth have strengthened our position as the fifth largest UK broadband provider, and positioned us as the largest domain name and hosting provider to the small and medium size business market. In addition, they have broadened our service portfolio and widened the geographical reach of the business, significantly extending the physical infrastructure of the group. Most importantly, each acquisition has brought new skills, incremental efficiencies and economies of scale. Our focus during 2004 has been to reposition our product set, and continue to integrate and build a business for future growth. This task continues today.

Customers and products

Last year I outlined our product mix; today, with these acquisitions and strong organic growth, our product mix is even better balanced, with a weighting in the high growth areas of the market.

This has led to the second phase in the Company's evolution, allowing us to focus on our three main customer groupings together with the products that our customers want:

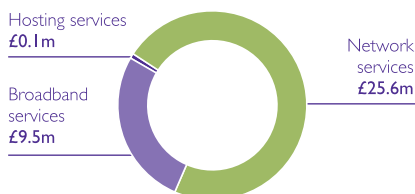
Customer	Residential	Small and medium businesses	Major and corporate business
<b>Products</b>			
Broadband services	✓	✓	✓
Hosting services	✓	✓	✓
Network services	—	✓	✓

# PROVIDING ACCESS

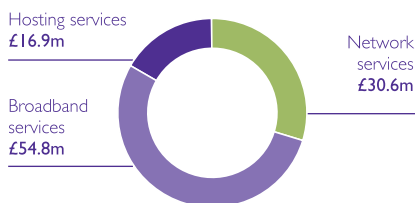


The revenue mix by product group:

2003: £35.2m



2004: £102.3m



## Customers and products CONTINUED

### Broadband services

Our Broadband business has grown to 192,000 customers, and continues to grow. We see Broadband (ADSL) as the access method which will allow us to focus on Broadband services, (services that can be carried over the Broadband pipe), and it is for that reason we have introduced our Security, Voice over IP (VoIP) and Voice over Broadband products, together with the opportunity for customers to buy hosting and domain names.

### Hosting services

Our Hosting business for small and medium size companies has continued to grow during 2004. We have continued to modify and update the product set and add new features and services to meet customer requirements. We currently sell bundled Domain Name and Shared Hosting, together with software applications, and provide customers with a product evolution path towards high-end dedicated servers. In response to customer demand, we added new Microsoft products to the portfolio, thus enabling customers to choose either Linux or Microsoft as the Shared Server platform. During 2005, we will enhance this product range to provide our residential customers with services they require.

### Network services

It is in this area that the "Altnets" have typically focused in the past, with Leased Lines and Voice services. As outlined last year, we reduced our dependencies on what are now termed "Old Wave" revenues (today these represent less than 25% of our business), and we have focused our Network Service business on network solutions with gigabit ethernet services, MPLS and VPNs, as well as complex hosting solutions.

Our secure data centres, resilient network and advanced security products have enabled us to attract a number of high profile customers from all market sectors including finance, entertainment and IT.

### Engineering and integration

The integration programme will continue to form an important part of our development and, during 2004, the process of integration through a range of programmes has moved forward swiftly. Important areas being addressed include the optimisation of the infrastructure, alignment of back office system (BOS), and portfolio management with business process enhancement.

We have continued to enhance and develop the network on which all our services are carried, and the new PIPEX network is built



## ENSURING QUALITY

using the very best of breed of suppliers for each specific task, ensuring the resulting service offering is robust, secure and highly available. PIPEX maintains excellent partnerships with Juniper, Cisco and Cienna, thus ensuring timely support and advice on potential issues.

For our Broadband customers, we continue to use BT's IPStream network because of its reliability, ease of use and ubiquity. During 2004, we reviewed our option on Local Loop Unbundling (LLU), and concluded that, during 2004 and early 2005, it was not the correct option for us. This decision was supported by the arrival of new LLU wholesalers in the UK that are happy to partner. We will review this again during 2005.

For our Hosting and Network Service customers, we have our own network, enabling us to provide the levels of service and customisation demanded. This network has more than 100 points of presence (PoPs) in towns and cities around the UK; PIPEX is able, therefore, to offer cost effective and truly resilient Internet connectivity to all users, as well as build Virtual Private Networks (VPNs) for those clients who require secure connectivity between offices. The PIPEX network resides upon a meshed, high-speed, fibre network that is completely resilient, operating at ten gigabits per second. Connectivity is taken

from multiple suppliers in order to guarantee fast and 'always on' service.

Security considerations are at the forefront of our network and operation. With the increased threat from organised crime, hackers and viruses, it is imperative that networks and services are designed to provide protection of all data carried on our networks. During the year, PIPEX has invested in leading edge technologies that identify and mitigate against organised attacks on our clients' services; this technology allows businesses to continue operating whilst being the subject of hostile attacks against their IT infrastructure. Our Security Committee ensures that threat assessments are carried out, and contingency plans developed and ready to deploy.

The enhancement of the PIPEX network has also delivered additional functionality and capability. Multi-protocol Label Switching (MPLS) is a service that provides a customer's traffic with a guaranteed Quality of Service (QoS). QoS allows applications such as Virtual Private Networks (VPNs) and real-time applications, including Voice Over Internet Protocol (VoIP) and Video broadcasting, to be deployed within the network.

Our German Hosting Business continues to perform according to plan and, with both



The PIPEX Communications' network

- SDH STM1/155Mbps
- Data centres
- Super POPs
- Access POPs
- Multiple access POPs
- Core backbone and peering POPs

the recent launch of the Dell Dedicated Server product, and the Shared Server and Domain business, it is providing valuable guidance on the behaviour of a different market and customer set.

#### Corporate responsibilities

PIPEX takes its corporate responsibilities very seriously and we adhere closely to the ISPA's 'Notice and take down procedure'. Like the rest of the industry, we have been working to make the Internet a safer place for its users – children in particular.

PIPEX has underlined its commitment to Internet security and the need to combat illegal online content by becoming a member of the Internet Watch Foundation (IWF). The IWF works with ISPs, telecommunications and software companies and Content Service Providers (CSPs) to reduce the availability of child abuse images, and criminally obscene and racist content. It influences and develops initiatives and programmes to combat online abuse, in partnership with UK Government departments, such as the Home Office and the Department of Trade and Industry.

PIPEX believes in providing the highest levels of customer service and satisfaction. We are constantly reviewing our services and processes in order to provide our customers

with the best Internet service available today. Should a customer require any assistance, PIPEX has dedicated Technical Support and Customer Service Teams that are staffed by highly trained, friendly people who are there to help.

#### PIPEX going forward

Our focus is on providing services to our business and residential customers across the UK and Germany. We plan to build upon the success of our marketing campaigns and continue to grow the brands for which we are known: PIPEX Internet, 123-reg, WebFusion, PIPEX Corporate Services, Nildram, and Host Europe in Germany.

Looking forward, we will continue to focus on our "New Wave" revenues, plus develop our mobile strategy using our WiMAX licences. As 75% of our business is generated from "on-line" sales, we are launching our new Portal ([www.pipex.com](http://www.pipex.com)) to offer customers easier access to our new products and services. With further enhancements, we will launch video and other content services.

For the major and corporate customers, PIPEX will build complex network solutions and provide a range of Internet access, hosting, voice, Oracle and security services and solutions, including managed virtual private networks (VPNs) and firewalls.

To provide these services, we will continue to use the latest technology and network elements under our "capex light" model.

We are therefore better placed than ever to address a wide target market in both the public and private sectors, covering a broad spectrum of customers from professional home users and home workers to large corporates.

**Mike Read** Chief Executive Officer  
8 April 2005



“THERE WAS NO BLINDING BY SCIENCE; PIPEX WAS FOCUSED ON EXPLAINING THE BUSINESS BENEFITS TO US”  
TOTTY CONSTRUCTION GROUP

**Transactions**

**Host Europe plc acquisition**

On 2 April 2004 the Company made a cash offer to Host Europe plc shareholders on the basis of 2.549p for each Host Europe share, valuing Host Europe at approximately £31.2m. Prior to making the offer, the Company had obtained irrevocable undertakings to accept the offer from certain Host Europe shareholders representing 39.3% of Host Europe's issued share capital. On the date of the offer, the Company purchased 155,480,000 Host Europe shares in the market at a price of 2.53p per share. This represented a further 13.2% of the issued share capital of Host Europe. On 27 April 2004 the offer was declared wholly unconditional, by which time the Company had received acceptances in respect of 81.25% of Host Europe's share capital.

The acquisition was financed by the issue of 314,285,715 new ordinary shares in the Company at a price of 10.5p per share, raising £33.0m (before expenses).

At 2 April 2004, the Company owned, or had commitments from Host Europe's shareholders to sell to the Company, shares representing 52.5% of Host Europe's share capital. In addition, the Company had, and had exercised, dominant influence over the financial and operating policies of the Host

Europe business. Consequently, Host Europe's results have been consolidated from 2 April.

The cost of the acquisition was £32.1m, including expenses. Net assets acquired were £2.9m giving rise to goodwill of £29.3m.

**AccentUK acquisition**

On 6 August 2004 the Company acquired AccentUK Limited, which trades as Nildram, for a total consideration of £13.0m in cash. The consideration was satisfied by increasing the Company's debt facilities with the Bank of Scotland.

The total acquisition cost was £14.4m and net liabilities acquired were £0.4m, giving rise to goodwill of £14.8m.

**Performance**

**Profit and loss**

Turnover for the year was £102.3m representing an increase of 190% over 2003. Turnover from existing operations has increased by 123% to £78.4m from a combination of organic growth and the full year impact of the 2003 acquisitions. Turnover from acquisitions of £23.9m represented the post-acquisition revenues of Host Europe and Nildram.

As a result of the acquisitions over the last year, it has now become appropriate for the Company to provide a segmental analysis of

its business. Broadband services incorporates the Company's full broadband offering including associated voice and security services. Customers in this segment range from residential to corporate. Turnover has increased from £9.5m in 2003 to £54.8m in 2004 as a result of consolidating a full twelve months' turnover for PIPEX Internet, the acquisition of Nildram and organic growth in Broadband.

Hosting services comprise shared hosting, dedicated hosting and co-location and include domain name registrations and applications software. Turnover in this segment rose with the acquisition of Host Europe in April, from a very low base to deliver £16.9m in 2004.

Network services are targeted at the higher end of the small and medium enterprise market and at corporate customers. The core products in the segment are access (private circuits, MPLS, VPNs, gigabit ethernet, symmetrical DSL and dial), voice (carrier pre-select and VOIP) and high-end hosting. Given the target market, customer numbers for Network services are much lower than for the other segments but with much higher average revenues per customer. Network services revenues accounted for 30% of turnover for 2004.

Gross profit in 2004 was £48.5m, representing a margin on sales of 47.4%. This is an increase

of 3.9 percentage points over last year, driven by the influence of higher relative margin hosting services in the turnover mix. This can be seen in the gross profit contributed by acquisitions in the year which, at £15.1m, represents a margin of 63.3%. The gross margin of 42.6% in existing operations was broadly unchanged from the previous year (2003: 42.3%).

Operating expenses, excluding depreciation, amortisation and a UITF 17 charge of £0.5m (2003: £0.6m), increased in the year by £17.8m to £37.1m, reflecting the impact of the operating costs in the businesses acquired in 2004 and the full year impact of prior year acquisitions. Measured as a percentage of turnover, there has been a dramatic improvement in operating expenses, falling from 53.4% in 2003 to 35.7% in 2004. As anticipated in last year's Report and Accounts, this reflects the success the business integration programme has had in eliminating unnecessary and overlapping costs, as acquired businesses are progressively assimilated into the group. In 2004, the group incurred costs (included in operating expenses) of £1.7m (2003: £0.4m), in relation to its business integration activities.

Adjusted EBITDA\* (EBITDA excluding the business integration costs and UITF 17 charge) is therefore a profit of £13.6m against an equivalent 2003 Adjusted EBITDA\* loss of £2.9m. Reported EBITDA for 2004 is a profit of £11.1m compared with a loss of £4.0m in 2003.

The increase in depreciation charge in the year was £2.1m, to £5.8m. Of this increase, £1.7m arose in the 2004 acquisitions.

There was a steep increase in net interest payable in the year from £0.5m in 2003 to £1.7m in 2004. As reported in the 2003 Report and Accounts, the acquisition of PIPEX Internet at the end of October 2003

was partly funded by a new debt facility of £15.0m with Bank of Scotland. The 2004 interest charge includes a full twelve months cost of servicing this debt. In addition, the Nildram acquisition added a further £13.0m to the debt facility in August 2004.

Adjusted PBT (excluding amortisation, integration costs and UITF 17 charges) was therefore a profit of £6.2m compared to an equivalent Adjusted loss before tax of £7.2m in 2003.

The 2004 results include a goodwill amortisation charge of £8.7m (2003: £1.7m). Goodwill on acquisitions is written off over ten years. The principal driver for the increase is PIPEX Internet which had a full twelve months goodwill amortisation in 2004, amounting to £4.9m, compared to a two month charge in 2003, amounting to £0.8m. In addition, goodwill arising on the 2004 acquisitions amounted to £44.0m which, given the timing of the transactions, increased the amortisation cost by a further £2.8m. On the basis of the group's amortisation policy, the on-going annual charge will be £10.5m.

As previously reported, at the time of the PIPEX Internet acquisition certain directors and senior managers were granted share options and warrants at the placing price of 6.25p. The grants were made on dates adjacent to the date of placing by which time the share price had moved up by 1.12p. A similar situation arose at the time of the Host Europe acquisition except that the placing price was 10.5p and the price at date of grant was 11.37p. Under UITF 17 the Company is required to account for the notional increase in value through the Profit and Loss account, apportioning the charge across the estimated vesting period. This gave rise to a UITF 17 charge of £577,000 in 2003, £451,000 in 2004 and is expected to result in an estimated charge in 2005 of £1,012,000.

The loss for the year was £5.3m (2003: loss of £9.9m) of which an operating profit of £1.0m arose in the acquired businesses.

#### Balance sheet

The total carrying value of goodwill as at 31 December 2004 was £94.6m (2003: £63.2m), with goodwill arising on the two 2004 acquisitions of £44.0m. The principal component of the goodwill balance is PIPEX Internet, with a carrying value of £47.9m.

Tangible fixed assets comprising buildings, plant, machinery and office equipment, have increased by £5.3m to £21.6m, of which £4.4m is attributable to the companies acquired in 2004.

When Firstnet Services Limited ("Firstnet") was acquired in August 2003 one of its assets was a Public Fixed Wireless Access licence granting exclusive use of spectrum at 3.6 – 4.2GHz covering the UK. This frequency range is adjacent to, and overlaps, the range identified by the WiMAX Forum as compatible spectrum. WiMAX is an emerging technology that will deliver broadband connectivity in large geographic areas (compared to WiFi) enabling high speed services to business customers and DSL-equivalent access to residential users. In the provisional acquisition balance sheet of Firstnet prepared for the purposes of the 2003 financial statements this licence had no carrying value attributed to it. The Company is required to finalise its fair value assessment in respect of the Firstnet acquisition in these 2004 financial statements and the directors have accordingly re-visited the fair value of this licence. In assessing the value of this asset at the acquisition date the Company has taken account of the significant progress, particularly in terms of specifying WiMAX global standards, that has been achieved in the post acquisition

\* Note: EBITDA represents operating profit or loss before depreciation and amortisation. Adjusted EBITDA is defined as EBITDA excluding integration costs and UITF 17 charges. A reconciliation of Adjusted EBITDA to EBITDA and reported operating loss is set out on page 10.

**Performance CONTINUED**

**Balance sheet continued**

period and of the uncertainties present in the exploitation of new technology. The value now attributed to the licence at the date of acquisition is £5.0m and this has reduced the goodwill arising in Firstnet by the same amount. The licence value is being amortised over twenty years.

The increase in debtors in the year, from £9.3m to £16.5m, is less than the proportional increase in billing over the same period, reflecting an improvement in debtor days outstanding. This is driven by the increasing trend towards direct debit or credit card payment methods.

Creditors falling due within one year also increased in line with acquisitions, which accounted for £9.2m of the increase. Longer term creditors comprise bank loans of £21.2m and obligations under finance leases of £1.7m. The increase in the total bank loans to £27.0m (2003: £16.9m) arose as a result of financing the Nildram acquisition, net of repayments.

**Cash flow**

Cash balances at the year end, including restricted deposits, were £11.3m (2003: £13.3m). The Company was free cash flow

positive in 2004, generating a cash inflow of £1.3m (2003: free cash outflow of £9.3m). Free cash flow is the cash flow before management of liquid resources, financing and acquisitions. Of the net cash outflow of £2.0m for the year, acquisitions accounted for £40.9m, repayments of loans £4.4m and repayment of finance leases £3.5m, offset by the funds raised from the issue of share capital of £32.6m (net of expenses but also including the exercise of share options), and the drawdown of a new loan of £13.0m.

Net debt at the year end was £20.6m (2003: £11.7m) comprising balance sheet cash of £11.3m less, the term loan of £25.2m, consideration loan notes of £2.0m, property mortgage of £1.8m, and outstanding lease obligations of £2.9m.

**Treasury**

The group uses financial instruments to raise finance for its operations and to manage risk arising from those operations. The group does not undertake any speculative trading in financial instruments.

Half of the forward interest obligation with respect to the term loan was swapped from variable rate to fixed rate.

On 8 November 2004 the then outstanding term loan from Bank of Scotland of £25.2m was syndicated such that Bank of Scotland remained as lender with £15.2m of the facility and Lloyds TSB were introduced as a new lender, on the same terms as in the existing facility, with £10.0m.

In the year £1.5m loan notes issued in relation to the Transigent acquisition in 2002 were redeemed.

**Stewart Porter** Chief Financial Officer  
8 April 2005

<b>*Reconciliation of Adjusted EBITDA to operating loss</b>		
	2004	2003
	£000	£000
<b>Operating profit/(loss) before amortisation, depreciation, UITF 17 charge and integration costs ("Adjusted EBITDA")</b>	<b>13,612</b>	<b>(3,073)</b>
Integration costs	(1,749)	(391)
UITF 17 charge	(451)	(577)
<b>Operating profit/(loss) before amortisation and depreciation ("EBITDA")</b>	<b>11,412</b>	<b>(4,041)</b>
Depreciation	(5,852)	(3,736)
Amortisation of goodwill and other intangible assets	(9,001)	(1,726)
<b>Operating loss</b>	<b>(3,441)</b>	<b>(9,503)</b>

## DIRECTORS

### Peter Dubens Chairman

Peter Dubens has experience in the start-up, development and restructuring of businesses both in the public and private sectors. He has led the consolidation strategy that has built PIPEX Communications plc to where it is today. Peter Dubens is also Executive Chairman of ukbetting plc, the largest UK online sports content and gaming company. He is also the co-founder of Palmer Capital Management, a hedge fund introductory business, and a number of other privately held companies.

### Mike Read Chief Executive Officer

Mike has thirty years' experience in the communications and Internet industry. He started his career in British Telecom where he gained considerable experience in international activities including: product management, product development, engineering & planning, marketing and advertising. This culminated in him working in the USA in the joint venture with MCI where he led the operational and engineering aspects of Concert. He later returned to the UK to become 'Chief of Global Engineering' which covered all engineering aspects of BT worldwide (with the exception of the UK).

During the initial 'launch phase' of the Internet Mike left BT and joined ANS in the USA – one of the first Internet companies which had just been purchased by AOL. His responsibilities covered sales, marketing, product management and business development.

In 1998 he moved to Florida to become CEO of Pacer International, a company that designed and built communication networks and systems for clients worldwide. Mike was headhunted by Pacer to run as President and COO of a consumer ISP 'roll up' in the USA called One Main. During the first eighteen months over 30 companies were purchased and rolled into one company.

In 2000 Mike moved back to the UK to become CEO/MD of XO Europe, the UK arm of which was acquired by GX Networks in October 2002.

### Stewart Porter Chief Financial Officer

Stewart Porter is a Chartered Accountant and holds a Bachelor of Science degree in electrical engineering. Prior to founding Zipcom (now PIPEX Communications) as Chief Financial Officer, Stewart was Finance Director for Highpoint Telecommunications Inc, a Canadian listed company, where he was closely involved in the successful establishment of a number of European start-ups. Stewart worked for Cable & Wireless for eight years in a number of senior financial positions, most recently as Director of Finance and Business Development in Global Markets, the business unit responsible for serving the multinational customers of Cable & Wireless.

### Christina Kennedy Non-executive director

Christina Kennedy has a Masters Degree in Business Administration and is a Fellow of the Chartered Institute of Secretaries. For over twenty years she has worked on a consultancy basis at Board level acting as Company Secretary in a variety of listed companies: AIM, top 250 and overseas companies with a secondary listing.

Industry experience is wide ranging including manufacturing, leisure and service companies. She has a good working knowledge of Stock Exchange Regulations, company law and corporate governance. She has also worked in a consultancy capacity as Corporate Governance Advisor for a major UK pension fund and therefore has a good understanding of investors' governance requirements. Her experience has involved her working with boards on acquisitions; restructuring; board compositions and appointments; directors' service contracts and remuneration issues; long-term incentive schemes; share options and risk management issues related to internal control requirements.

### Laurence Blackall Non-executive director

A former Chairman of the Internet Service Providers' Association (ISPA), Laurence Blackall has a Masters Degree in Marketing and over twenty years' experience in the media and telecommunications industries. After an early career that included Virgin and the SEMA Group he was a director of Frost & Sullivan and a Vice President at McGraw-Hill. In 1995 he founded Global Internet and took it public as Internet Technology Group in 1996.

He managed the sale of his company to Concentric Network Corporation, which was itself acquired by XO Communications Inc. Together with Peter Dubens, he acquired XO's UK business, which was, in turn, acquired by Zipcom plc. This was renamed GX Networks plc, before becoming PIPEX Communications plc in 2003.

# DIRECTORS' REPORT

The directors present their annual report and the audited financial statements for the year ended 31 December 2004.

## Principal activity and business review

The principal activity of the group during the period was the supply of telecommunication services. A detailed review of the business is set out in the Chairman's statement on pages 2 and 3, the business review on pages 4 to 7 and the financial review on pages 8 to 10.

## Financial results and dividends

The results for the group for the year are shown in the profit and loss account on page 22.

The directors do not recommend the payment of a dividend.

## Directors and directors' interests

The directors who held office during the year were as follows:

Peter Dubens	Chairman
Michael Read	Chief Executive Officer
Stewart Porter	Chief Financial Officer
David Rickards	Chief Operating Officer (resigned 1 April 2004)
Christina Kennedy	non-executive
Laurence Blackall	non-executive

Peter Dubens and Laurence Blackall retire by rotation in accordance with the Articles of Association and being eligible, offer themselves for re-election.

The directors' remuneration and the interests of the directors in the share capital of the Company are detailed in the report on directors' remuneration on pages 16 to 19.

## Employees

It is the policy of the group that there should be no unfair discrimination in recruiting and promoting staff, including applicants who are disabled. The directors are committed to maintaining and developing communication and consultation processes with employees, who in turn are encouraged to develop an awareness of the issues affecting the group. The directors place considerable emphasis on employees sharing in the success of the group. This is achieved through the performance related bonus Scheme and participation in the share option Schemes. The Company is establishing an Employee Consultation Forum in line with the Information and Consultation of Employees Regulatory Directive. This Forum has elected representatives from employee constituencies and will meet at least twice annually with the Company's senior management to discuss business issues.

## Substantial shareholdings

As of 8 April 2005 the Company had been notified of the following significant shareholdings:

	%
UBS Warburg	17.26
P Dubens	6.36
L Blackall	6.36
Chase Nominees Limited	6.11
M&G Recovery IF3 Fund	4.58
Bank of New York Nominees Limited	3.15

#### **Policy on payment to suppliers**

Where the supply of goods and services is satisfactory and in the absence of any dispute, the group and Company's policy is to pay suppliers in accordance with the terms agreed prior to the supply of goods and services. Where no such agreement exists the group and Company's policy is to pay suppliers in accordance with the terms contained in the invoice. Trade creditors at 31 December 2004 as a proportion of amounts invoiced by suppliers during the period represent 51 days (2003: 45 days) for the existing business and 40 days for the acquired businesses. The Company has no material trade creditors.

#### **Political and charitable contributions**

The Company made no contributions for political or charitable purposes during the year.

#### **Environmental policy**

The group's environmental policy is to meet the statutory requirements placed upon it and to apply good environmental practice in its operations whilst recognising that it is contractually obliged to meet its customers requirements.

#### **Annual General Meeting**

The Annual General Meeting will be held on 7 June 2005 at 2.00pm at the offices of Financial Dynamics, Holborn Gate, 26 Southampton Buildings, London WC2A 1PB.

#### **Auditors**

In accordance with Section 385 of the Companies Act 1985, a resolution proposing that KPMG Audit Plc be re-appointed as auditors of the group will be put to the Annual General Meeting.

This report was approved by the Board on 8 April 2005.

**Stewart Porter** Chief Financial Officer

The Board is responsible to shareholders for effective direction and control of the group and this report describes the framework for corporate governance and internal control that the directors have established to enable them to carry out this responsibility. It also explains how the Company has applied the Principles of Good Governance. Although, as an AIM listed company, the Company is not required to comply with the provisions of the Combined Code ("the Code") and this is not a statement of compliance as required by the Code, the Board of directors recognises the importance of, and is committed to, ensuring that effective corporate governance procedures relevant to smaller listed companies are in place.

### The Board and Committees

At 1 January 2004 the Board comprised four executive directors (P Dubens, M Read, S Porter and D Rickards) and two non-executive directors (C Kennedy and L Blackall). On 1 April 2004 D Rickards resigned. At 31 December 2004 the Board therefore comprised three executive and two non-executive directors. The Board considers that the current composition provides a reasonable balance of independence. L Blackall, while a substantial shareholder, brings an independent view of the telecoms industry to Board discussions. The Board however accepts that C Kennedy is considered to be the only current independent non-executive director as defined under the Code.

The Board, which meets on average six times a year, is responsible for the overall strategy and financial performance of the group and has a formal schedule of matters reserved for its approval. Each Board meeting is preceded by a clear agenda and any relevant information is provided to directors in advance of the meeting.

Since September 2003 the roles of Chairman and Chief Executive Officer have been separated. The Board does not consider it necessary to appoint a senior independent director.

The Remuneration Committee comprises C Kennedy and L Blackall only and is chaired by C Kennedy. The report on directors' remuneration on pages 16 to 19 contains a detailed description of remuneration and applicable policies.

Given the small size of the Board, and as permitted by the Code, the Board has not appointed a Nominations Committee. The Board as a whole considers the appointment of all directors and senior managers. The Articles of Association of the Company require directors to submit themselves for re-election at the first Annual General Meeting following appointment and then every three years by rotation, but in accordance with good practice one third of the directors will be submitted for re-election each year.

The Audit Committee comprises L Blackall (Chairman) and C Kennedy. C Kennedy is considered by the Board to have relevant financial experience. The Committee operates under written terms of reference and meets at least twice a year with the Company's external auditors, and the executive directors present by invitation only. The Committee meets with the external auditors without the executive directors present as it considers appropriate. The Committee is responsible for the independent monitoring of the effectiveness of the system of internal control, compliance, accounting policies and published financial statements on behalf of the Board. This is achieved primarily through a review of the annual financial statements and a review of the nature and scope of the external audit. Any significant findings or identified risks are examined so that appropriate action may be taken. The Committee is also responsible for keeping under review the independence and objectivity of the external auditors, including a review of non-audit services provided to the group, consideration of any relationships with the Company that could affect independence, and seeking written confirmation from the auditors that, in their professional judgement, they are independent.

### Relations with shareholders

The Company encourages the participation of both institutional and private investors. Communication with private individuals is maintained through the Annual General Meeting (AGM), and annual and interim reports. In addition further details on the strategy and performance of the Company can be found at its website ([www.pipex.net](http://www.pipex.net)) which includes copies of the Company's press releases.

The Company's share registrars provide a helpdesk, which members may contact with enquiries regarding their shareholdings. The helpdesk telephone number is 0870 162 3100 (or 0044 20 8639 2157 for overseas callers) and their e-mail address [ssd@capitaregistrars.com](mailto:ssd@capitaregistrars.com).

### Internal control

The Board has overall responsibility for the group's systems of internal control and for monitoring their effectiveness. Although no system of internal control can provide absolute assurance against material mis-statement or loss, the group's systems are designed to provide the directors with reasonable assurance that issues are identified on a timely basis and dealt with appropriately.

The group has an established organisational structure with clearly defined lines of authority, responsibility and accountability, which is reviewed regularly. Group management are responsible for the identification and evaluation of key risks applicable to their areas of business.

The external auditors are engaged to express an opinion on the accounts. They review and test the systems of internal financial controls and data contained in the accounts, and discuss with management the reporting of operational results and the financial condition of the group, to the extent necessary to express their audit opinion.

The Board has considered the need for an internal audit function, but has resolved that due to the size of the group, this cannot be justified on the grounds of cost effectiveness at present.

### Directors' and officers' liability insurance and indemnity

The Company has purchased insurance to cover its directors and officers against the costs of defending themselves in legal proceedings taken against them in that capacity, and in respect of any damages resulting in those proceedings. The Company also indemnifies its directors and officers to the extent permitted by law. Neither the insurance nor the indemnity provide cover where the director has acted fraudulently or dishonestly.

### Going concern

The directors, having made appropriate enquiries, consider that the Company and the group have adequate resources to continue in operational existence for the foreseeable future and therefore it is appropriate to adopt the going concern basis in preparing the accounts on pages 22 to 48.

# BOARD REPORT ON DIRECTORS' REMUNERATION

## Remuneration Committee

The Remuneration Committee comprises C Kennedy (Chairman) and L Blackall.

The Committee meets not less than twice a year to determine all aspects of the remuneration of the executive directors and other senior managers. The fees of the non-executive directors are determined by the Board as a whole. No director or employee has a role in determining his own remuneration.

## Remuneration policy

The Committee determines overall policy for executive remuneration. The Committee sets levels of remuneration to attract, retain and motivate executive directors and other senior managers and, in doing so, takes into account the level of remuneration throughout the telecommunications industry. Employees throughout the group, including executive directors, have performance reviews annually.

The main components of the executive directors' and senior managers' remuneration are:

- a competitive base salary
- an annual performance bonus
- pension provision
- benefits in kind
- share options

The group operates a discretionary bonus Scheme. The Scheme applies to directors, senior managers and certain other employees. Individual payments made under the Scheme are generally dependent on the Company achieving its financial targets and the attainment of individual objectives.

The group makes contributions to money purchase personal pension Schemes on behalf of certain executive directors and senior managers.

Other customary benefits, such as car allowances, permanent health insurance and life assurance are made available as appropriate.

The group has three share options Schemes, the Unapproved Executive Share Option Scheme, the Approved Executive Share Option Scheme and the EMI Scheme. Details of options granted under these Schemes are given in note 19 to the financial statements.

## Directors' service contracts

The service contracts of executive directors remain in force until age 65, or age 60 in the case of the Chairman, and continue until terminated by either party giving to the other not less than twelve months' written notice.

The service contracts of non-executive directors remain in force until terminated by either party giving to the other not less than three months' written notice.

## Directors' remuneration

	Salaries and fees £'000	Benefits £'000	Bonus £'000	Total 2004 £'000	Total 2003 £'000	Pension 2004 £'000	Pension 2003 £'000
<b>Executive</b>							
M Read	223	—	150	373	105	21	2
S Porter	181	—	125	306	283	29	24
P Dubens	225	—	125	350	342	—	—
<b>Non-executive</b>							
L Blackall	25	—	—	25	18	—	—
C Kennedy	25	—	—	25	17	—	—
<b>Former directors</b>							
D Rickards	51	3	—	54	27	—	—
G Purvis	—	—	—	—	284	—	29
J Richards (non-executive)	—	—	—	—	38	—	—
	730	3	400	1,133	1,114	50	55

The bonus received by M Read, S Porter and P Dubens was in respect of services during the year.

Shareholdings and option interests of the directors in office at 31 December 2004 are as follows:

## Directors' shareholdings

	1p ordinary shares at 31 December 2004	1p ordinary shares at 31 December 2003
M Read	—	—
S Porter	174,500	174,500
P Dubens	138,888,889	138,888,889
L Blackall	138,888,889	138,888,889
C Kennedy	167,800	125,000

## Directors' share options

	Note	At 1 January 2004	Awarded during the year	Cancelled during the year	At 31 December 2004	Exercise price	Exercise period
S Porter	(i)	989,130	—	—	<b>989,130</b>	1.00p	20 November 2001 to 19 November 2011
	(ii)	2,693,583	—	—	<b>2,693,583</b>	1.00p	20 November 2001 to 19 November 2011
	(iii)	5,253,000	—	—	<b>5,253,000</b>	4.50p	27 December 2001 to 26 December 2011
	(ii)	2,602,440	—	—	<b>2,602,440</b>	3.00p	27 December 2001 to 26 December 2011
	(i)	3,455,313	—	—	<b>3,455,313</b>	2.25p	20 February 2003 to 19 February 2013
	(iv)	17,939,247	—	—	<b>17,939,247</b>	2.25p	20 February 2003 to 19 February 2013
	(ii)	750,000	—	—	<b>750,000</b>	3.00p	20 February 2003 to 19 February 2013
M Read	(v)	1,600,000	—	—	<b>1,600,000</b>	6.25p	24 October 2003 to 23 October 2013
	(ii)	9,650,000	—	—	<b>9,650,000</b>	6.25p	24 October 2003 to 23 October 2013
P Dubens	(v)	1,600,000	—	—	<b>1,600,000</b>	6.25p	24 October 2003 to 23 October 2013
	(ii)	8,400,000	—	—	<b>8,400,000</b>	6.25p	24 October 2003 to 23 October 2013
L Blackall		—	—	—	—		
C Kennedy		—	—	—	—		
D Rickards		—	—	—	—		

(i) EMI Scheme – no performance criteria attached

(ii) Unapproved Scheme – no performance criteria attached

(iii) Unapproved Scheme – only exercisable once the Company's market capitalisation reaches £25.0 million.

(iv) Unapproved Scheme – 10,697,280 are only exercisable when the Company's share price reaches 5.00p and it is EBITDA positive, measured on a monthly basis. The remaining 7,236,967 are only exercisable once the Company's share price reaches 3.00p and the Company is EBITDA positive, measured on a monthly basis

(v) EMI Scheme – only exercisable once the Company's share price reaches 9.00p and the Company is EBITDA positive, measured on a monthly basis.

No directors in office at 31 December 2004 exercised any share options during the year.

### Directors' share options CONTINUED

At 31 December 2004 directors of the Company held the following warrants over ordinary shares in the Company:

	Warrants	Exercise price
M Read	15,000,000	6.25p
P Dubens	50,000,000	6.25p
M Read	10,000,000	10.50p
M Read	10,000,000	10.50p
P Dubens	17,500,000	10.50p
P Dubens	17,500,000	10.50p
S Porter	2,500,000	10.50p
S Porter	2,500,000	10.50p

The above warrants at 6.25p can only be exercised after 1 January 2005, when the Company is EBITDA positive for a twelve month period and the Company's share price has reached 12p.

Warrants at 10.5p are exercisable in two stages. 50% may be exercised when the Company's share price has reached 16p and the remaining 50% on the share price reaching 21p.

The mid-market price for the Company's shares at 31 December 2004 was 7.76p. The high and low mid-market prices of the ordinary shares during the year to 31 December 2004 were 12p and 6.88p respectively.

On behalf of the Board

**Stewart Porter** Chief Financial Officer

8 April 2005

## STATEMENT OF DIRECTORS' RESPONSIBILITIES

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and group and of the profit or loss for that period. In preparing those financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the group will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

# REPORT OF THE INDEPENDENT AUDITORS

to the members of PIPEX Communications plc



## KPMG Audit Plc

8 Salisbury Square  
London EC4Y 8BB  
United Kingdom

We have audited the financial statements on pages 22 to 48.

This report is made solely to the Company's members, as a body, in accordance with Section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by the law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

### Respective responsibilities of directors and auditors

The directors are responsible for preparing the Annual Report and Accounts. As described on page 20 this includes responsibility for preparing the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established by statute, the Auditing Practices Board and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' report is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and transactions with the group is not disclosed.

We read the other information accompanying the financial statements, and consider whether it is consistent with those statements. We consider the implications for our report if we become aware of any apparent mis-statements or material inconsistencies with the financial statements.

### Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material mis-statement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

### Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and the group as at 31 December 2004 and of the loss of the group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc Chartered Accountants and Registered Auditor  
8 April 2005

# CONSOLIDATED PROFIT AND LOSS ACCOUNT

for the year ended 31 December 2004

	Note	Existing operations 2004 £'000	Acquisitions 2004 £'000	Total 2004 £'000	2003 £'000
<b>Turnover</b>	1, 2	<b>78,437</b>	<b>23,852</b>	<b>102,289</b>	35,218
Cost of sales		(45,014)	(8,760)	(53,774)	(19,893)
<b>Gross profit</b>		<b>33,423</b>	<b>15,092</b>	<b>48,515</b>	15,325
Operating expenses before amortisation, depreciation and integration costs		(26,251)	(9,103)	(35,354)	(18,975)
Amortisation of intangibles		(6,191)	(2,810)	(9,001)	(1,726)
Depreciation		(4,139)	(1,713)	(5,852)	(3,736)
Integration costs		(1,318)	(431)	(1,749)	(391)
Operating expenses		(37,899)	(14,057)	(51,956)	(24,828)
Operating profit before amortisation, depreciation and integration costs		7,172	5,989	13,161	(3,650)
Amortisation of intangibles		(6,191)	(2,810)	(9,001)	(1,726)
Depreciation		(4,139)	(1,713)	(5,852)	(3,736)
Integration costs		(1,318)	(431)	(1,749)	(391)
<b>Operating loss</b>	3	<b>(4,476)</b>	<b>1,035</b>	<b>(3,441)</b>	(9,503)
Other interest receivable and similar income	5			465	79
Interest payable and similar charges	6			(2,058)	(469)
<b>Loss on ordinary activities before taxation</b>				<b>(5,034)</b>	(9,893)
Tax on loss on ordinary activities	7			(29)	—
<b>Loss for the financial year</b>				<b>(5,063)</b>	(9,893)
Loss per ordinary share – basic	26			0.25p	0.89p
– diluted	26			0.25p	0.89p

The loss on a historic cost basis is the same as the results reported above.

All of the results above relate to continuing operations.

# CONSOLIDATED STATEMENT OF GROUP TOTAL RECOGNISED GAINS AND LOSSES

for the year ended 31 December 2004

	Note	2004 £'000	2003 £'000
Loss for the financial year		(5,063)	(9,893)
Translation difference in respect of net investment in overseas subsidiary undertaking	23	60	—
<b>Total recognised losses in the year</b>		<b>(5,003)</b>	(9,893)

# CONSOLIDATED BALANCE SHEET

at 31 December 2004

	Note	2004 £'000	2004 £'000	2003 £'000	2003 £'000
<b>Fixed assets</b>					
Intangible assets					
Positive goodwill	8	94,714		63,522	
Negative goodwill	8	(94)		(319)	
Patents	8	8		9	
Wireless licence	8	4,667		—	
			99,295		63,212
Tangible assets	9		21,581		16,264
			120,876		79,476
<b>Current assets</b>					
Stock	11	21		218	
Debtors	12	16,386		9,264	
Cash at bank and in hand	13	11,309		13,267	
		27,716		22,749	
<b>Creditors: amounts falling due within one year</b>	14	<b>(44,094)</b>		<b>(36,476)</b>	
<b>Net current liabilities</b>			<b>(16,378)</b>		<b>(13,727)</b>
<b>Total assets less current liabilities</b>			<b>104,498</b>		<b>65,749</b>
<b>Creditors: amounts falling due after one year</b>	15	<b>(22,861)</b>		<b>(13,541)</b>	
<b>Provisions for liabilities and charges</b>	16	<b>(2,251)</b>		<b>(828)</b>	
<b>Net assets</b>			<b>79,386</b>		<b>51,380</b>
<b>Capital and reserves</b>					
Called up share capital	19, 23		21,822		18,141
Share capital to be issued	23		—		2,540
Share premium account	23		83,868		52,451
Other reserves	23		10,703		10,252
Profit and loss account	23		(37,007)		(32,004)
<b>Equity shareholders' funds</b>			<b>79,386</b>		<b>51,380</b>

The accounts on pages 22 to 48 were approved by the Board of directors on 8 April 2005 and were signed on its behalf by:

Peter Dubens Chairman

Stewart Porter Chief Financial Officer

# COMPANY BALANCE SHEET

at 31 December 2004

	Note	2004 £'000	2004 £'000	2003 £'000	2003 £'000
<b>Fixed assets</b>					
Investments	10		64,799		18,099
<b>Current assets</b>					
Debtors	12	65,114		56,807	
Cash at bank and in hand	13	2,126		5,932	
		67,240		62,739	
<b>Creditors: amounts falling due within one year</b>	14	<b>(39,528)</b>		<b>(27,395)</b>	
<b>Net current assets</b>			27,712		35,344
<b>Total assets less current liabilities</b>					
Creditors due after more than one year	15		(21,200)		(12,000)
<b>Provisions for liabilities and charges</b>	16		<b>(192)</b>		<b>(287)</b>
<b>Net assets</b>			71,119		41,156
<b>Capital and reserves</b>					
Called up share capital	19, 23		21,822		18,141
Share capital to be issued	23		—		2,540
Share premium account	23		83,868		52,451
Other reserves	23		10,496		10,045
Profit and loss account	23		(45,067)		(42,021)
<b>Equity shareholders' funds</b>			71,119		41,156

The accounts on pages 22 to 48 were approved by the Board of directors on 8 April 2005 and were signed on its behalf by:

Peter Dubens Chairman

Stewart Porter Chief Financial Officer

# CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 December 2004

	Note	2004 £'000	2003 £'000
<b>Cash inflow/(outflow) from operating activities</b>	24	<b>7,643</b>	<b>(7,553)</b>
<b>Returns on investment and servicing of finance</b>			
Interest paid		(1,523)	(83)
Interest received		465	79
Interest element of finance lease payments		(377)	(217)
		<b>(1,435)</b>	<b>(221)</b>
<b>Taxation received/(paid)</b>		<b>217</b>	<b>(344)</b>
<b>Capital expenditure and financial investment</b>			
Purchase of tangible fixed assets		(6,086)	(1,245)
Proceeds from disposals of tangible fixed assets		939	93
		<b>(5,147)</b>	<b>(1,152)</b>
<b>Acquisitions</b>			
Purchase of subsidiary undertakings	21	(40,695)	(39,745)
Prior year acquisitions	22	(163)	—
		<b>(40,858)</b>	<b>(39,745)</b>
<b>Cash outflow before management of liquid resources and financing</b>		<b>(39,580)</b>	<b>(49,015)</b>
<b>Management of liquid resources</b>			
Cash withdrawn from term deposits		—	250
Movement in restricted deposits		(693)	54
<b>Financing</b>			
Issue of ordinary share capital		33,000	45,169
Expenses on issue of ordinary share capital		(1,227)	(1,933)
Exercise of share options		785	99
Repayment of loan notes		(1,501)	—
Drawdown of new loan		13,000	15,000
Repayment of loan		(2,890)	(40)
Capital element of finance lease payments		(3,545)	(1,381)
<b>Net cash inflow from financing</b>		<b>37,622</b>	<b>56,914</b>
<b>(Decrease)/increase in cash in the period</b>		<b>(2,651)</b>	<b>8,203</b>

# CONSOLIDATED CASH FLOW STATEMENT CONTINUED

for the year ended 31 December 2004

## Reconciliation of net cash flow to movement in net debt

for the year ended 31 December 2004

	2004 £'000	2003 £'000
<b>(Decrease)/increase in cash in period</b>	<b>(2,651)</b>	<b>8,203</b>
Net movement in liquid resources	693	(304)
Payment of loan note	1,501	—
Drawdown of new loan	(13,000)	(15,000)
Repayment of loan	2,890	40
Cash outflow from lease financing	3,545	1,381
Change in net debt resulting from cash flows	(7,022)	(5,680)
New finance leases	(486)	—
Finance leases acquired with subsidiary	(504)	(3,126)
Finance lease fair value adjustment (see note 22)	(950)	—
Conversion of loan stock	—	1,570
Loans acquired with subsidiary	—	(1,919)
Movement in net debt	(8,962)	(9,155)
Opening net debt	(11,655)	(2,500)
<b>Closing net debt</b>	<b>(20,617)</b>	<b>(11,655)</b>

## Analysis of net debt

at 31 December 2004

	At 1 January 2004 £'000	Cashflow £'000	Acquisitions (excluding cash) £'000	Other £'000	At 31 December 2004 £'000
Cash	10,842	(2,651)	—	—	8,191
Restricted deposits	2,425	693	—	—	3,118
<b>Cash at bank and in hand per balance sheet</b>	<b>13,267</b>	<b>(1,958)</b>	<b>—</b>	<b>—</b>	<b>11,309</b>
Bank loans	(16,879)	(10,110)	—	—	(26,989)
Finance leases	(4,553)	3,545	(504)	(1,436)	(2,948)
Loan notes	(3,490)	1,501	—	—	(1,989)
<b>Net debt</b>	<b>(11,655)</b>	<b>(7,022)</b>	<b>(504)</b>	<b>(1,436)</b>	<b>(20,617)</b>

The movement of £1,436,000 in Other relates to new finance leases of £486,000 and a fair value adjustment on finance leases of £950,000 (see note 22).

## RECONCILIATION OF MOVEMENTS IN SHAREHOLDERS' FUNDS

for the year ended 31 December 2004

	Group 2004 £'000	Group 2003 £'000	Company 2004 £'000	Company 2003 £'000
<b>Loss for the financial year</b>	<b>(5,063)</b>	(9,893)	<b>(3,046)</b>	(20,450)
New share capital subscribed (net of issue costs)	<b>32,558</b>	51,905	<b>32,558</b>	51,905
Share capital to be issued	—	2,540	—	2,540
Translation difference in respect of net investment in overseas subsidiary undertaking	<b>60</b>	—	—	—
Granting of options/UITF 17 charge reversed	<b>451</b>	577	<b>451</b>	577
<b>Net increase in shareholders' funds</b>	<b>28,006</b>	45,129	<b>29,963</b>	34,572
Opening shareholders' funds	<b>51,380</b>	6,251	<b>41,156</b>	6,584
<b>Closing shareholders' funds</b>	<b>79,386</b>	51,380	<b>71,119</b>	41,156

# NOTES TO THE FINANCIAL STATEMENTS

## I Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the group's financial statements.

### Basis of preparation

The financial statements have been prepared in accordance with applicable accounting standards and under the historical cost convention.

The cost of acquisitions represents the cash value of the consideration and the market value of the shares issued on the date the offer became unconditional, plus expenses.

### Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiary undertakings made up to 31 December 2004. Unless otherwise stated, the acquisition method of accounting has been adopted. Under this method, the results of subsidiary undertakings acquired in the year are included in the consolidated profit and loss account from the date of acquisition.

The group financial statements consolidate the financial statements of PIPEX Communications plc and all its subsidiary undertakings. As permitted by Section 230 of the Companies Act 1985, a separate profit and loss account is not presented in respect of the Company.

### Going concern

The group has financed its trading losses from cash raised from share placings. As at 31 December 2004 the group had cash of £11,309,000 including £3,118,000 of restricted cash. The directors continue to monitor the group's funding strategy and have prepared detailed forecasts for future periods. These forecasts underpin the going concern basis, which the directors have applied in the preparation of the financial statements for the year ended 31 December 2004.

### Turnover

Turnover comprises the value of telecommunication and related services provided net of value added tax. Income is recognised in the period in which the service is provided.

### Goodwill

When the fair value of the consideration for an acquired undertaking exceeds the fair value of its separable net assets, the difference is treated as purchased goodwill and is capitalised and amortised through the profit and loss account over its estimated useful life. The economic life of goodwill has been estimated by the directors to be ten years.

Where the fair value of the separable net assets exceeds the fair value of the consideration for an acquired undertaking the difference is treated as negative goodwill and is capitalised and amortised through the profit and loss account in the period in which the non-monetary assets acquired are recovered. In the case of fixed assets this is the period over which they are depreciated, and in the case of current assets, the period over which they are sold or otherwise realised. The economic life of negative goodwill has been estimated by the directors to be four years.

### Other intangible assets and amortisation

Amortisation is provided to write off the cost of intangible assets by equal instalments over their estimated useful economic lives as follows:

Wireless licence	Twenty years
Patents	Ten years

Intangible assets acquired as part of an acquisition are capitalised at their fair value where this can be measured reliably.

## I Accounting policies CONTINUED

### Tangible fixed assets and depreciation

Depreciation is provided to write off the cost less the estimated residual value of tangible fixed assets by equal instalments over their estimated useful economic lives as follows:

Network infrastructure	Two to ten years
Indefeasible rights of use	Life of the contract
Office equipment	Three to five years
Leasehold improvements	Life of the lease
Plant and machinery	Three to five years

Where assets are financed under finance leases the cost is written off over the shorter of the lease term and the remaining useful economic life.

### Investment in subsidiary undertakings

Investments in subsidiary undertakings are initially stated at cost in the balance sheet of the Company unless, in the opinion of the directors, there has been an impairment, in which case an appropriate adjustment is made.

### Foreign currencies

Transactions in foreign currencies are recorded using the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated using the rate of exchange ruling at the balance sheet date and the gains or losses on translation are included in the profit and loss account.

### Leases

Assets acquired under finance leases are capitalised and the outstanding future lease obligations are shown in creditors. Operating lease rentals are charged to the profit and loss account on a straight line basis over the period of the lease.

### Pension costs

The pension costs charged in the profit and loss account represent the amounts of contributions payable to the group's defined contribution pension Schemes in the accounting period.

### Share options

The cost of awards to employees that take the form of shares or rights to shares are recognised over the period of the employee's related performance.

### Taxation

The charge for taxation is based on the results for the period and takes into account taxation deferred because of timing differences between the treatment of certain items for taxation and accounting purposes.

Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed, by the balance sheet date, except as required by FRS 19.

### Cash and liquid resources

Cash, for the purpose of the cash flow statement, comprises cash in hand and deposits repayable on demand, less overdrafts payable on demand. Cash for the purpose of the balance sheet includes short-term deposits and restricted deposits.

Liquid resources comprise current asset investments held as readily disposable stores of value as defined by Financial Reporting Standard I (Revised 1996) Cash Flow Statements. Liquid resources held in both the current and preceding year include restricted bank deposits.

## 2 Segmental information

The group operates one class of business, that of telecommunication services, and consequently does not prepare segmental information by class of business. However, to provide useful additional information, turnover is subdivided into three main service categories shown below.

	2004 £'000	2003 £'000
<b>Turnover</b>		
Broadband services	54,797	9,517
Hosting services	16,894	79
Network services	30,598	25,622
	<b>102,289</b>	<b>35,218</b>

Turnover and loss before interest and tax, together with net assets by country of origin, are set out below.

	Net assets 2004 £'000	Net assets 2003 £'000	Turnover 2004 £'000	Turnover 2003 £'000	(Loss)/profit before interest and tax 2004 £'000	Loss before interest and tax 2003 £'000
UK	77,803	51,380	98,096	35,218	(3,601)	(9,503)
Germany	1,383	—	4,193	—	160	—
	<b>79,186</b>	<b>51,380</b>	<b>102,289</b>	<b>35,218</b>	<b>(3,441)</b>	<b>(9,503)</b>

Turnover analysed by destination is not materially different to turnover by origin.

## 3 Operating loss

	2004 £'000	2003 £'000
<b>Operating loss is stated after charging/(crediting):</b>		
Auditors' remuneration:		
– audit	215	120
– other services	107	40
Depreciation and other amounts written off tangible fixed assets:		
– owned assets	3,280	1,729
– under finance leases	2,572	2,007
(Profit)/loss on disposal of fixed assets	(53)	15
Amortisation of		
– negative goodwill (see note 8)	(225)	(225)
– positive goodwill (see note 8)	8,892	1,950
– patents (see note 8)	1	1
– wireless licence (see note 8)	333	—
Rentals payable under operating leases		
– land and buildings	2,246	1,120
– other operating leases	1,014	1,455
UITF 17 charge	451	577

The auditors' remuneration includes £18,000 (2003: £17,500) for the Company. Remuneration for non-audit services represents fees for tax compliance and advice. In addition £195,000 of fees were paid to the auditors in connection with the acquisition of AccentUK Limited. These are included in the cost of investment.

#### 4 Staff numbers and costs

The average number of persons (including executive directors) employed by the group during each year was as follows:

	2004 Number	2003 Number
Full time operations staff	446	219
Executive and administrative	128	71
	<b>574</b>	<b>290</b>

The aggregate payroll costs (including directors' remuneration) were as follows:

	2004 £'000	2003 £'000
Wages and salaries	18,751	11,317
Share related awards	451	577
Social security costs	2,164	1,329
Pension costs	468	343
	<b>21,834</b>	<b>13,566</b>

Remuneration of directors:

	2004 £'000	2003 £'000
Emoluments for services as a director	1,133	926
Compensation for loss of office	—	188
Pension contributions	50	55
	<b>1,183</b>	<b>1,169</b>

Emoluments of the highest paid director (excluding pension contributions) were £373,000 (2003: £342,000). Amounts paid by the group in respect of their pension contributions were £21,000 (2003: £nil).

Details of pension contributions are set out in note 20 to the accounts. See the board report on directors' remuneration on pages 16 to 19 for further details.

#### 5 Other interest receivable and similar income

	2004 £'000	2003 £'000
Bank interest receivable	465	79

#### 6 Interest payable and similar charges

	2004 £'000	2003 £'000
Interest payable on finance leases	377	217
Bank interest payable	1,523	196
Loan note interest payable	158	56
	<b>2,058</b>	<b>469</b>

**7 Tax on ordinary activities**

	2004 £'000	2003 £'000
United Kingdom corporation tax at 30% (2003: 30%)	—	—
Overseas tax on profit for the year	29	—
<b>Total current tax</b>	<b>29</b>	<b>—</b>

**Reconciliation of the group's current tax charge to the United Kingdom statutory rate**

	2004 £'000	2003 £'000
Loss on ordinary activities before tax	(5,034)	(9,893)
Loss on ordinary activities at standard rate of UK corporation tax of 30% (2003: 30%)	(1,510)	(2,968)
Non deductible amortisation	2,700	518
Capital allowances in excess of depreciation	(16)	(151)
Permanent disallowable items	57	401
Difference between UK and overseas standard tax rates	(5)	—
Utilisation of tax losses brought forward	(1,197)	—
Other timing differences, including unrelieved tax losses carried forward	—	2,200
<b>Total current tax (as above)</b>	<b>29</b>	<b>—</b>

At 31 December 2004 there were unrelieved losses in the group of approximately £75.5m (2003: £79.5m).

**Deferred tax**

The amounts of unrecognised deferred taxation assets comprise:

	2004 £'000	2003 £'000
Unrelieved tax losses	22,650	23,847
Unclaimed capital allowances	—	893
	<b>22,650</b>	<b>24,740</b>

The above figures are subject to the agreement of corporation tax computations with the relevant tax authorities.

## 8 Intangible fixed assets

Group	Wireless licence £'000	Positive goodwill £'000	Negative goodwill £'000	Patents £'000	Total £'000
<b>Cost</b>					
At 1 January 2004	—	65,624	(901)	10	64,733
Additions (see note 21)	—	44,028	—	—	44,028
Fair value adjustments (see note 22)	5,000	(3,944)	—	—	1,056
<b>At 31 December 2004</b>	<b>5,000</b>	<b>105,708</b>	<b>(901)</b>	<b>10</b>	<b>109,817</b>
<b>Amortisation</b>					
At 1 January 2004	—	2,102	(582)	1	1,521
Charge for the year	333	8,892	(225)	1	9,001
<b>At 31 December 2004</b>	<b>333</b>	<b>10,994</b>	<b>(807)</b>	<b>2</b>	<b>10,522</b>
<b>Net book value</b>					
<b>At 31 December 2004</b>	<b>4,667</b>	<b>94,714</b>	<b>(94)</b>	<b>8</b>	<b>99,295</b>
At 31 December 2003	—	63,522	(319)	9	63,212

Negative goodwill arose on the acquisition of HighwayOne Corporation Limited in 2001. This negative goodwill is being released over the related period of expense of the non-monetary assets acquired, that being four years. Positive goodwill arising in the year relates to the acquisitions of Host Europe plc and AccentUK Limited (see note 21), and is being amortised over ten years. The Wireless Licence was acquired with Firstnet Services Limited and is being amortised over twenty years and is stated at a directors' valuation at the acquisition of Firstnet on 28 August 2003. The valuation takes account of the progress, particularly in terms of specifying WiMAX global standards, that has been achieved in the post acquisition period and of the uncertainty present in the exploitation of new technology. (Please refer to pages 9 and 10).

The Company held no intangible fixed assets at 31 December 2004 or 31 December 2003.

**9 Tangible fixed assets**

Group	Freehold buildings £'000	Leasehold improvements £'000	Network infrastructure £'000	Office equipment £'000	Plant and machinery £'000	Total £'000
<b>Cost</b>						
At 1 January 2004	2,087	1,542	19,978	404	71	24,082
Acquisitions (see note 21)	—	530	2,093	990	745	4,358
Additions	—	116	6,502	616	309	7,543
Disposals	—	—	(1,612)	—	(36)	(1,648)
Fair value adjustment (see note 22)	—	2	20	—	12	34
Exchange difference	—	—	116	42	6	164
<b>At 31 December 2004</b>	<b>2,087</b>	<b>2,190</b>	<b>27,097</b>	<b>2,052</b>	<b>1,107</b>	<b>34,533</b>
<b>Depreciation</b>						
At 1 January 2004	32	246	7,341	187	12	7,818
Charge for the year	85	306	4,785	443	233	5,852
Disposals	—	—	(746)	—	(16)	(762)
Exchange difference	—	—	20	21	3	44
<b>At 31 December 2004</b>	<b>117</b>	<b>552</b>	<b>11,400</b>	<b>651</b>	<b>232</b>	<b>12,952</b>
<b>Net book value</b>						
<b>At 31 December 2004</b>	<b>1,970</b>	<b>1,638</b>	<b>15,697</b>	<b>1,401</b>	<b>875</b>	<b>21,581</b>
At 31 December 2003	2,055	1,296	12,637	217	59	16,264

Included in the total net book value of £21,581,000 are assets of £2,539,000 held under finance leases as follows: network infrastructure £2,462,000 (2003: £2,746,000), office equipment £12,000 (2003: £nil) and plant and machinery £65,000 (2003: £nil). Depreciation for the year on these assets was as follows: network infrastructure £2,394,000 (2003: £2,007,000), office equipment £118,000 (2003: £nil) and plant and machinery £60,000 (2003: £nil).

The Company held no tangible fixed assets at 31 December 2004 or 31 December 2003.

## 10 Fixed asset investments

Company	Interest in subsidiary undertakings £'000
<b>Cost</b>	
1 January 2004	18,839
Additions	46,700
<b>At 31 December 2004</b>	<b>65,539</b>
<b>Amounts provided</b>	
1 January 2004	740
<b>At 31 December 2004</b>	<b>740</b>
<b>Net book value</b>	
<b>At 31 December 2004</b>	<b>64,799</b>
At 31 December 2003	18,099

Additions in the year of £46,700,000 relate to the acquisition of Host Europe plc and AccentUK Limited (see note 21).

The Company's principal subsidiary undertakings included in the financial statements are as follows:

Name	Proportion of ordinary share capital held	Nature of business/activity
PIPEX Internet Limited <sup>(i)</sup> (formerly Zipcom Telecommunications Limited)	100%	Telecommunications
HighwayOne Limited	100%	Telecommunications
GXN Limited	100%	Holding company
PIPEX Communications Services Limited	100%	Telecommunications
PIPEX Communications One Limited <sup>(ii)</sup> (formerly PIPEX Communications UK Limited)	100%	Telecommunications
Compulink Information eXchange Limited	100%	Telecommunications
XTML Limited	100%	Telecommunications
PIPEX Communications Business Solutions Limited <sup>(i)</sup>	100%	Telecommunications
AccentUK Limited	100%	Telecommunications
Nildram Communications Limited <sup>(iii)</sup> (formerly Nildram Limited)	100%	Telecommunications
Trinité Limited	100%	Telecommunications
PIPEX Communications Hosting Limited (formerly Host Europe Limited)	100%	Telecommunications
Host Europe GmbH	100%	Telecommunications

(i) directly held by the Company

(ii) on 1 February 2005 the name of the Company was changed from PIPEX Communications UK Limited

(iii) on 1 February 2005 the name of the Company was changed from Nildram Limited

All subsidiary undertakings are registered in England and Wales with the exception of GXN Limited which is registered in Scotland and Host Europe GmbH which is registered in Germany. All subsidiaries operate in the UK with the exception of Host Europe GmbH which operates in Germany. A full list of the Company's subsidiaries will be given in the next annual return.

**11 Stock**

	Group 2004 £'000	Group 2003 £'000	Company 2004 £'000	Company 2003 £'000
Finished goods for sale	21	218	—	—

**12 Debtors**

	Group 2004 £'000	Group 2003 £'000	Company 2004 £'000	Company 2003 £'000
Trade debtors	7,188	5,747	—	—
Amounts due from subsidiary undertakings	—	—	64,863	56,787
Corporation tax	—	178	—	—
Taxation and social security	—	—	—	20
Other debtors	1,079	843	79	—
Prepayments and accrued income	8,119	2,496	172	—
	<b>16,386</b>	<b>9,264</b>	<b>65,114</b>	<b>56,807</b>

Included in group prepayments and accrued income are rent deposits of £356,000 (2003: £117,000) which are recoverable after more than one year.

**13 Cash at bank and in hand**

Cash at bank and in hand comprises cash in hand, deposits repayable on demand and restricted deposit accounts.

Included in group cash at bank and in hand are funds of £2,100,000 (2003: £2,024,000) held in a restricted deposit account in respect of a guarantee over the first loan note (see note 14).

Also included within cash at bank and in hand are £520,000 (2003: £80,000) of deposits with credit card companies. Of this sum £219,000 will be accessed within twelve months.

Also included within cash at bank and in hand are £328,000 (2003: £321,000) of funds in restricted deposit accounts. These amounts relate to lease contracts over telecommunications equipment. Of this sum, £198,000 was released on 1 April 2005 while the remaining £130,000 will be released within the next twelve months.

A further £170,000 (2003: £nil) is held in restricted deposit as a guarantee over future rental payments. This sum cannot be accessed within the next twelve months.

The balance of group cash at bank and in hand, being £8,191,000 (2003: £10,842,000) is held in current accounts, overnight money market accounts and no-notice deposit accounts.

Cash at bank and in hand per the Company balance sheet comprises £2,100,000 (2003: £2,024,000) held in a restricted deposit account (see above) and £26,000 (2003: £3,908,000) held in current accounts, overnight money market accounts and no-notice deposit accounts.

#### 14 Creditors: amounts falling due within one year

	Group 2004 £'000	Group 2003 £'000	Company 2004 £'000	Company 2003 £'000
Bank loans (see notes 15,18)	5,789	4,879	3,975	3,000
Loan notes (see note 18)	1,989	3,490	1,989	3,490
Obligations under finance leases (see note 15)	1,287	3,012	—	—
Trade creditors	18,791	14,272	1,052	—
Amounts owed to group undertakings	—	—	32,307	20,620
Taxation and social security	2,299	822	27	—
Other creditors	556	269	155	—
Corporation tax	68	—	—	—
Accruals and deferred income	13,315	9,732	23	285
	<b>44,094</b>	<b>36,476</b>	<b>39,528</b>	<b>27,395</b>

Loan notes issued in respect of the acquisition of Transigent Limited are as follows:

First consideration loan note – £1,989,000.

The first consideration loan note is fully guaranteed and carries interest at a rate of 0.5% below base lending rate.

#### 15 Creditors: amounts falling due after one year

	Group 2004 £'000	Group 2003 £'000	Company 2004 £'000	Company 2003 £'000
Bank loan (see note 18)	21,200	12,000	21,200	12,000
Obligations under finance leases	1,661	1,541	—	—
	<b>22,861</b>	<b>13,541</b>	<b>21,200</b>	<b>12,000</b>

Bank loans are repayable as follows:

	Group 2004 £'000	Group 2003 £'000	Company 2004 £'000	Company 2003 £'000
Within one year	5,789	4,879	3,975	3,000
Between two and five years	21,200	12,000	21,200	12,000
	<b>26,989</b>	<b>16,879</b>	<b>25,175</b>	<b>15,000</b>

The bank loan of £25,175,000 carries interest at a rate of LIBOR +2.75%.

The bank loan of £1,814,000 carries interest at a rate of bank base rate +1.35%. As a result of the acquisition of Firstnet Services Limited (now called PIPEX Communications Business Solutions Limited) the loan became repayable within one year.

**15 Creditors: amounts falling due after one year** CONTINUED

The maturity of obligations under finance leases is as follows:

Group	2004 £'000	2003 £'000
Within one year	1,287	3,012
In the second to fifth years	1,661	1,541
	<b>2,948</b>	<b>4,553</b>

The Company does not hold any assets under finance leases.

**16 Provisions for liabilities and charges**

Group	Onerous leases £'000	Dilapidations £'000	UITF25 £'000	Other £'000	Total £'000
At 1 January 2004	479	50	287	12	828
Arising on the acquisition of subsidiary undertakings (see note 21)	—	—	25	—	25
Fair value adjustment (see note 22)	2,201	—	—	—	2,201
Arising during the year	—	—	128	—	128
Utilised during the year	(670)	—	(249)	(12)	(931)
<b>At 31 December 2004</b>	<b>2,010</b>	<b>50</b>	<b>191</b>	<b>—</b>	<b>2,251</b>

The UITF 25 provision relates to National Insurance payable on exercise of share options. This will be utilised as and when the share options are exercised. The onerous leases provision includes £1,842,000 in respect of an acquired telecommunications contract and will be utilised up to the end of the contract in August 2010. The remaining onerous lease provision of £168,000 relates to rental costs for a vacant property and will be utilised up to the end of the lease in July 2005. Dilapidations relate to a vacant property and will be utilised at the expiry of the lease, being July 2005.

Company	2004 £'000
At 1 January 2004	287
Arising during the year	128
Utilised during the year	(223)
<b>At 31 December 2004</b>	<b>192</b>

Provisions relate to the National Insurance payable on exercise of share options according to UITF 25. This will be utilised as and when the share options are exercised.

## 17 Operating leases

The group had commitments to make annual payments under non-cancellable operating leases which expire as follows:

	Short leasehold property 2004 £'000	Other 2004 £'000	Short leasehold property 2003 £'000	Other 2003 £'000
Within one year	543	1,198	—	1,486
Within two to five years	1,116	767	957	71
After five years	538	163	436	—
	<b>2,197</b>	<b>2,128</b>	1,393	1,557

In addition to the above, the group had an annual commitment in respect of telecom circuits of £11,134,000 (2003: £7,266,000). Typically these leases are twelve months in length and cancellable at seven days' notice following the end of the initial twelve month period.

## 18 Financial instruments

The group's financial instruments comprise cash and liquid resources, and various items such as trade debtors and trade creditors that arise directly from its operations. The main purpose of the financial instruments is to provide finance for the group's operations.

Where it is considered appropriate, the group enters into derivative transactions (principally forward foreign currency transactions). The purpose of such transactions is to manage the currency and interest rate risks arising from the group's operations and its sources of finance.

It is the group's policy that no speculative trading in financial instruments shall be undertaken.

The main risks arising from the group's financial instruments are interest rate risk, liquidity risk and foreign currency risk. The directors review and agree policies for managing each of these risks, and they are summarised below.

As permitted by Financial Reporting Standard 13, short-term debtors and creditors have been excluded from the following disclosures (with the exception of note (iii)).

### (i) Interest rate risk

The group financed its operations throughout the year from bank deposits. During the year £16.75 million of the forward interest payment obligations with respect to the £26.5 million bank loan were swapped from fixed to variable rate. The interest rate exposure of the financial assets of the group as at 31 December was:

	Fixed 2004 £'000	Floating 2004 £'000	Nil 2004 £'000	Total 2004 £'000
Sterling	5,559	5,499	176	11,234
US\$	—	14	—	14
Euro	—	61	—	61
	<b>5,559</b>	<b>5,574</b>	<b>176</b>	<b>11,309</b>
	Fixed 2003 £'000	Floating 2003 £'000	Nil 2003 £'000	Total 2003 £'000
Sterling	2,104	11,037	—	13,141
US\$	79	47	—	126
Euro	—	—	—	—
	<b>2,183</b>	<b>11,084</b>	<b>—</b>	<b>13,267</b>

**18 Financial instruments** CONTINUED

## (i) Interest rate risk CONTINUED

The interest rate exposure of the financial liabilities of the group as at 31 December was:

	Fixed 2004 £'000	Floating 2004 £'000	Nil 2004 £'000	Total 2004 £'000
Sterling	16,000	12,978	2,948	31,926
	Fixed 2003 £'000	Floating 2003 £'000	Nil 2003 £'000	Total 2003 £'000
Sterling	1,501	18,868	4,553	24,922

## (ii) Liquidity risk

The group's objective is to ensure adequate funding for its operations ahead of commitments being made for expansion. This has been achieved in the current year through the issue of equity.

	Debt 2004 £'000	Other financial liabilities 2004 £'000	Total 2004 £'000
Financial liabilities maturing:			
in one year or less or on demand	7,778	1,287	9,065
in more than one year but not more than two years	5,300	1,464	6,764
in more than two years but not more than five years	15,900	197	16,097
	<b>28,978</b>	<b>2,948</b>	<b>31,926</b>
	Debt 2003 £'000	Other financial liabilities 2003 £'000	Total 2003 £'000
Financial liabilities maturing:			
in one year or less or on demand	8,369	3,012	11,381
in more than one year but not more than two years	3,750	756	4,506
in more than two years but not more than five years	8,250	308	8,558
after five years	—	477	477
	<b>20,369</b>	<b>4,553</b>	<b>24,922</b>

## (iii) Foreign currency risk

The group has occasional transactional currency exposures. Such exposures mainly arise from purchases in US dollars and Euros.

## 18 Financial instruments CONTINUED

### (iv) Fair values

The following table sets out the book values and estimated fair values of the group's financial instruments:

	Book value 2004 £'000	Fair value 2004 £'000	Book value 2003 £'000	Fair value 2003 £'000
Primary financial instruments:				
Cash at bank and in hand	11,309	11,309	13,267	13,267
Bank loans	(26,989)	(26,989)	(16,879)	(16,879)
Loan notes	(1,989)	(1,989)	(3,490)	(3,490)
Finance leases due within one year	(1,287)	(1,287)	(3,012)	(3,012)
Finance leases due after more than one year	(1,661)	(1,661)	(1,541)	(1,541)
	<b>(20,617)</b>	<b>(20,617)</b>	<b>(11,655)</b>	<b>(11,655)</b>

## 19 Called up share capital

### Authorised and allotted share capital

	2004 £'000	2003 £'000
<b>Authorised</b>		
Equity: 4,000,000,000 ordinary shares of 1p each		
At 1 January 2004	30,000	15,000
Authorised during the year	10,000	15,000
<b>At 31 December 2004</b>	<b>40,000</b>	<b>30,000</b>
<b>Allotted, called up and fully paid</b>		
Equity: ordinary shares of 1p each		
At 1 January 2004	18,141	7,100
Issued during the year	3,681	11,041
<b>At 31 December 2004</b>	<b>21,822</b>	<b>18,141</b>

On 27 April 2004 the authorised share capital was increased by 1,000 million 1p ordinary shares.

Share capital issued at nominal value in the year relates to the exercise of share options (30,719,332 shares for consideration of £784,671), shares allocated in respect of the previous year's acquisition of Firstnet Services Limited (23,092,369 shares at a fair value of £2,540,161) and shares placed during the year (314,285,715 shares for cash consideration of £33,000,000).

**19 Called up share capital CONTINUED**

## Share options

At 31 December 2004 rights to options over 193,091,713 ordinary shares of the Company were outstanding as follows:

	At 1 January 2004	Granted	Exercised/ lapsed	Cancelled	At 31 December 2004	Exercise price	Exercise period
Unapproved Scheme	6,751,591	—	(4,058,008)	—	<b>2,693,583</b>	1.00p	20.11.2001 to 19.11.2011
	10,506,000	—	(5,253,000)	—	<b>5,253,000</b>	4.50p	27.12.2001 to 26.12.2011
	5,204,880	—	(2,602,440)	—	<b>2,602,440</b>	3.00p	27.12.2001 to 26.12.2011
	1,500,000	—	(750,000)	—	<b>750,000</b>	3.00p	20.11.2001 to 19.11.2011
	35,878,494	—	(17,939,247)	—	<b>17,939,247</b>	2.25p	20.03.2003 to 19.03.2013
	27,374,000	—	—	—	<b>27,374,000</b>	6.25p	24.10.2003 to 19.03.2013
	10,000,000	—	—	—	<b>10,000,000</b>	6.25p	28.10.2003 to 27.10.2013
		75,350,000	—	—	<b>75,350,000</b>	10.5p	21.06.2004 to 20.06.2014
		10,000,000	—	—	<b>10,000,000</b>	8.5p	04.08.2004 to 03.08.2014
		21,500,000	—	—	<b>21,500,000</b>	7.5p	20.10.2004 to 19.10.2014
EMI Scheme	989,130	—	—	—	<b>989,130</b>	1.00p	20.11.2001 to 19.11.2011
	650,000	—	—	—	<b>650,000</b>	3.00p	20.02.2003 to 19.02.2013
	3,455,313	—	—	—	<b>3,455,313</b>	2.25p	20.02.2003 to 19.02.2013
	13,160,000	1,500,000	(125,000)	—	<b>14,535,000</b>	6.25p	24.10.2003 to 23.10.2013
	<b>115,469,408</b>	<b>108,350,000</b>	<b>(30,727,695)</b>	—	<b>193,091,713</b>		

## Share warrants

At 1 January 2004 and 31 December 2004 there were outstanding warrants to subscribe to up to 75,000,000 shares of the Company. These warrants can only be exercised when the Company is EBITDA positive for the previous months and the Company's share price has reached 12p.

On 27 April 2004 warrants to subscribe to up to 60,000,000 ordinary shares of the Company were issued and were outstanding at 31 December 2004. These warrants are exercisable in two stages. 50% may be exercised when the Company's share price has reached 16p and the remaining 50% when the share price has reached 21p.

**20 Pension scheme**

The group does not operate an occupational pension scheme but makes a percentage contribution of qualifying salary to certain employees' personal pension schemes. The amount charged to the profit and loss account in respect of such contributions was £468,000 (2003: £343,000).

The outstanding contributions to the pension scheme were £nil (2003: £nil).

## 21 Acquisitions

### (i) Summary

Below is a summary of the acquisitions made by PIPEX Communications plc in the year ended 31 December 2004.

	2004 £'000
Fair value of assets acquired	2,509
Goodwill	44,028
Consideration	46,537
Satisfied by:	
Cash	44,164
Costs of acquisition	2,373
	46,537
Effects on group cash flow:	
Cash consideration	44,164
Costs of acquisition	2,373
Cash balances on acquisition	(5,842)
Net cash outflow	40,695

### (ii) Host Europe

On 2 April 2004 PIPEX purchased 13.2% of the share capital of Host Europe plc on the open market. On the same date PIPEX made a public offer to the shareholders of Host Europe plc. This offer from PIPEX was accepted by the directors of Host Europe, their families and certain other employees (who together held 39.3% of Host Europe's share capital). These shareholders provided PIPEX with irrevocable undertakings to sell their shares. As a result, on 2 April 2004, PIPEX announced it had 'control' of over 52% of Host Europe's shares.

The cost of investment comprises £31.2 million to acquire 100% of the share capital of Host Europe plc and £0.9 million of professional fees. Goodwill of £29,250,000 arising on acquisition is being amortised over ten years, the useful life as estimated by the directors.

Host Europe contributed £15,980,000 of turnover in the period since acquisition, an operating profit of £1,088,000 (after goodwill amortisation of £2,194,000) and accounted for cash flows from operating activities of £2,507,000.

The turnover and operating profit of Host Europe between 1 January 2004 and 1 April 2004 were £5,085,000 and £715,000 respectively. Their net assets at 31 December 2003 were £12,927,000 and the operating loss for the year to 31 December 2003 was £134,000.

**21 Acquisitions CONTINUED**
**(ii) Host Europe CONTINUED**

Details of the fair values of the assets and liabilities acquired are provisional and are set out below:

	Book value of assets acquired £'000	Fair value adjustments £'000	Fair value £'000
Fixed assets	3,443	—	3,443
Stock	5	—	5
Debtors	1,579	(360)	1,219
Cash	5,584	—	5,584
Creditors (falling due within one year)	(7,169)	(181)	(7,350)
Provisions	(170)	145	(25)
<b>Net assets/(liabilities)</b>	<b>3,272</b>	<b>(396)</b>	<b>2,876</b>
Goodwill			29,250
<b>Consideration</b>			<b>32,126</b>
Satisfied by:			
Cash			31,198
Costs of acquisition			928
			<b>32,126</b>
Effects on group cash flow:			
Cash consideration and costs			32,126
Cash balances and acquisition			(5,584)
<b>Net cash outflow</b>			<b>26,542</b>

**EXPLANATORY NOTES:**
**Debtors**

The adjustment to debtors represents the removal of a previously recognised deferred tax asset.

**Creditors (falling due within one year)**

Creditors have been increased to accrue for all estimated outstanding liabilities.

**Provisions**

The fair value adjustment is to remove a dilapidation provision not expected to be required.

## 21 Acquisitions CONTINUED

### (iii) AccentUK Limited

On 6 August 2004 the group acquired AccentUK Limited and its subsidiaries, Trinité Limited, Nildram Limited and Trinité Services Limited.

The acquisition was financed by a bank loan of £13.0 million. Costs of acquisition were £1.4 million.

Goodwill of £14,778,000 arising on acquisition is being amortised over ten years, the useful life as estimated by the directors.

AccentUK contributed £7,872,000 of turnover in the period since acquisition, an operating loss of £53,000 (after goodwill amortisation of £616,000) and accounted for cash flows from operating activities of £1,123,000.

The turnover and operating profit of AccentUK between 1 January 2004 and 5 August 2004 were £9,694,000 and £400,000 respectively. Their net assets at 31 March 2004 were £323,000 and the operating loss for the year to 31 March 2004 was £179,000.

Details of the fair values of the assets and liabilities acquired are provisional and are set out below:

	Book value of assets acquired £'000	Fair value adjustments £'000	Fair value £'000
Fixed assets	915	—	915
Debtors	1,586	52	1,638
Cash	258	—	258
Creditors (falling due within one year)	(3,178)	—	(3,178)
<b>Net (liabilities)/assets</b>	<b>(419)</b>	<b>52</b>	<b>(367)</b>
Goodwill			14,778
<b>Consideration</b>			<b>14,411</b>
Satisfied by:			
Cash			12,966
Costs of acquisition			1,445
			<b>14,411</b>
Effects on group cash flow:			
Cash consideration and costs			14,411
Cash balances and acquisition			(258)
<b>Net cash outflow</b>			<b>14,153</b>

#### EXPLANATORY NOTES:

##### Debtors

Debtors have been adjusted to increase prepaid telecommunications rentals at acquisition.

**22 Goodwill on prior year acquisitions**

## (i) Summary

	Provisional fair value to the group 2003 £'000	Adjustments 2004 £'000	Final fair value to the group 2004 £'000
Fair value of net assets acquired	8,238	4,107	12,345
Goodwill	57,162	(3,944)	53,218
Consideration	65,400	163	65,563

## (ii) XTML Limited and Compulink Information eXchange Limited

	Provisional fair value to the group 2003 £'000	Adjustments 2004 £'000	Final fair value to the group 2004 £'000
Fair value of net assets acquired	(704)	(1,919)	(2,623)
Goodwill	1,732	2,019	3,751
Consideration	1,028	100	1,128

The adjustments to provisional fair values, and therefore goodwill, comprise predominantly the inclusion of a provision for an onerous lease relating to a telecommunications network in the amount of £2,021,000 and the release of £282,000 of accrued liabilities at acquisition. The adjustment to consideration is in respect of previously unprovided professional fees.

## (iii) Firstnet Services Limited

	Provisional fair value to the group 2003 £'000	Adjustments 2004 £'000	Final fair value to the group 2004 £'000
Fair value of net assets acquired	857	4,599	5,456
Goodwill	6,150	(4,592)	1,558
Consideration	7,007	7	7,014

The adjustments to provisional fair values, and therefore goodwill, comprise predominantly £5,000,000 in respect of a directors' valuation placed on the Wireless Licence at acquisition. (See pages 9, 10 and 33). Other adjustments include a write down of obsolete stock of £166,000, and £240,000 in respect of unaccrued liabilities. Fixed assets and lease creditors have been adjusted by £950,000 in respect of a previously unrecorded finance lease. The adjustment to consideration is in respect of previously unprovided professional fees.

## (iv) PIPEX Internet Limited

	Provisional fair value to the group 2003 £'000	Adjustments 2004 £'000	Final fair value to the group 2004 £'000
Fair value of net assets acquired	8,085	1,427	9,512
Goodwill	49,280	(1,371)	47,909
Consideration	57,365	56	57,421

The adjustment to provisional fair values, and therefore goodwill, relates to prepayments. This comprises £1,348,000 in prepaid customer telecommunications equipment and £79,000 in prepaid circuit costs. The adjustment to consideration is in respect of previously unprovided professional fees.

## 23 Reserves

Group	Share capital £'000	Shares to be issued £'000	Share premium account £'000	Other reserves £'000	Profit and loss account £'000	Total £'000
At 1 January 2004	18,141	2,540	52,451	10,252	(32,004)	51,380
Issue of shares	3,681	(2,540)	32,644	—	—	33,785
Issue costs	—	—	(1,227)	—	—	(1,227)
Grant of options	—	—	—	451	—	451
Gain on translation of foreign subsidiary	—	—	—	—	60	60
Retained loss for the year	—	—	—	—	(5,063)	(5,063)
<b>At 31 December 2004</b>	<b>21,822</b>	<b>—</b>	<b>83,868</b>	<b>10,703</b>	<b>(37,007)</b>	<b>79,386</b>

### Company

At 1 January 2004	18,141	2,540	52,451	10,045	(42,021)	41,156
Issue of shares	3,681	(2,540)	32,644	—	—	33,785
Issue costs	—	—	(1,227)	—	—	(1,227)
Grant of options	—	—	—	451	—	451
Retained loss for the year	—	—	—	—	(3,046)	(3,046)
<b>At 31 December 2004</b>	<b>21,822</b>	<b>—</b>	<b>83,868</b>	<b>10,496</b>	<b>(45,067)</b>	<b>71,119</b>

Other reserves consist of the following:

Group	Merger reserve £'000	Capital reserve £'000	UITF 17 reserve £'000	Other reserves £'000	Total £'000
At 1 January 2004	5,996	207	577	3,472	10,252
Grant of options	—	—	451	—	451
<b>At 31 December 2004</b>	<b>5,996</b>	<b>207</b>	<b>1,028</b>	<b>3,472</b>	<b>10,703</b>

### Company

At 1 January 2004	5,996	—	577	3,472	10,045
Grant of options	—	—	451	—	451
<b>At 31 December 2004</b>	<b>5,996</b>	<b>—</b>	<b>1,028</b>	<b>3,472</b>	<b>10,496</b>

The other reserves represent the premium on shares issued as part of the consideration for the acquisition of Transigent Limited.

The merger reserve represents share premium on shares issued to acquire XTML Limited, Compulink Information eXchange Limited and PIPEX Internet Limited.

**24 Reconciliation of operating loss to operating cash flows**

	2004 £'000	2003 £'000
Operating loss	(3,441)	(9,503)
Depreciation charge	5,852	3,736
Amortisation charge	9,001	1,726
(Profit)/loss on sale of fixed assets	(53)	16
UITF 17 charge (non-cash)	451	577
Decrease/(increase) in stock	35	(17)
(Increase)/decrease in debtors	(3,084)	841
Decrease in creditors	(315)	(4,878)
Decrease in provisions	(803)	(51)
<b>Net cash inflow/(outflow) from operating activities</b>	<b>7,643</b>	<b>(7,553)</b>

**25 Related party disclosures**

Peter Dubens, an executive director of the Company, is a director of the following companies:

Oakley Capital Limited which provided services to the group of £37,000 (2003: £21,000) of which £3,000 (2003: £nil) was outstanding at the year end. Oakley Capital Limited was also a customer of PIPEX and accounted for sales of £6,000 (2003: £6,000), of which £nil was outstanding at the year end.

ukbetting plc, a customer of PIPEX, which accounted for sales of £12,000 (2003: £20,000), of which £nil (2003: £2,000) was outstanding at the year end.

David Rickards, an executive director of the Company at the time, was also a director of Waycourt Estates Limited, which charged £70,000 (2003: £74,000), for the rental of premises occupied by a group company.

**26 Loss per share**

	Year ended 31 December 2004	Year ended 31 December 2003
Loss for the financial year attributable to shareholders	£5,063,000	£9,893,000
Weighted average number of equity shares in issue	2,063,093,735	1,106,864,224
Basic/diluted loss per equity share*	0.25p	0.89p

\*Since the conversion of potential ordinary shares to ordinary shares would decrease the net loss per share, they are not dilutive. Accordingly diluted loss per share is the same as basic loss per share.

# NOTICE OF ANNUAL GENERAL MEETING

Notice is hereby given that the 2005 Annual General Meeting of PIPEX Communications plc will be held at the offices of Financial Dynamics, Holborn Gate, 26 Southampton Buildings, London WC2A 1PB on 7 June 2005 at 2pm for the following purpose:

As ordinary business to consider and, if thought fit, pass Resolutions 1 to 4 inclusive below which will be proposed as Ordinary Resolutions:

1. To receive, approve and adopt the report of the directors and the financial statements of the Company for the financial year ended 31 December 2004 together with the report of the auditors thereon.
2. To re-elect Peter Dubens as a director, who retires by rotation pursuant to Article 102 of the Company's Articles of Association.
3. To re-elect Laurence Blackall as a director, who retires by rotation pursuant to Article 102 of the Company's Articles of Association.
4. To re-appoint KPMG Audit Plc as auditors to the Company to hold office from the conclusion of the meeting until the conclusion of the next Annual General Meeting and to authorise the directors to fix their remuneration.

As special business to consider and, if thought fit, to pass the following Resolutions of which Resolution 5 will be proposed as an Ordinary Resolution and Resolutions 6 and 7 will be proposed as Special Resolutions:

5. That:
  - (i) the authority to allot relevant securities and equity securities conferred on the directors by Article 8.2 of the Company's Articles of Association be and is hereby granted for the period ending on the date falling fifteen months after the passing of this Resolution or at the conclusion of the next Annual General Meeting of the Company to be held after the date of the passing of this Resolution whichever is the earlier (the "prescribed period"), and for the period the Section 80 amount shall be £7,250,000; and
  - (ii) all previous authorisations given by the Company in general meeting or otherwise pursuant to Section 80 of the Companies Act 1985 ("the Act") be and are hereby revoked to the extent not previously exercised.
6. That subject to the passing of Resolution 5 above, the power to allot relevant securities and equity securities conferred on the directors by Article 8.2 of the Company's Articles of Association be and is hereby granted for the prescribed period (as defined in Resolution 5 above) and for that period the Section 89 amount shall be £1,090,000. This authority and power shall revoke to the extent not previously exercised the power granted in this regard by the Company at the Extraordinary General Meeting held on 27 April 2004.
7. That the Company be and is hereby granted general and unconditional authority (pursuant to Section 166 of the Companies Act 1985 ("the Act") and the authorities contained in its Articles of Association) to make market purchases (as defined in Section 163 of the Act) of up to in aggregate 218,350,000 of its own ordinary shares of 1p each in the capital of the Company ("Ordinary Shares") provided that:
  - (i) the maximum price which may be paid for an Ordinary Share is an amount equal to not more than 5% above the average of the middle market quotations for the Ordinary Shares taken from the London Stock Exchange plc Daily Official List for the five business days before the day on which the purchase is made, and the minimum price which may be paid for an Ordinary Share is 1p, in each case exclusive of expenses payable by the Company; and
  - (ii) the authority conferred by this Resolution shall expire on the conclusion of the next Annual General Meeting of the Company held after the passing of this Resolution, or 7 June 2006 (whichever shall first occur), except that the Company may, before such expiry, enter into a contract for the purchase of its own Ordinary Shares which would or may require to be completed or executed wholly or partly after the expiration of this authority as if the said authority had not expired.

By order of the Board

**Stewart Porter**  
Company Secretary  
6 May 2005

**Registered Office:**  
Carlton House  
27A Carlton Drive  
London  
SW15 2BS

Registered in England No: 3974683

### Notes:

- (1) Any member entitled to attend and vote at the Annual General Meeting convened by this notice may appoint one or more proxies to attend and, on a poll, to vote instead of him. A proxy need not be a member of the Company.
- (2) To appoint a proxy, the form enclosed with this notice should be completed and deposited at the offices of the Company's registrars not less than 48 hours before the meeting time of the Annual General Meeting specified above.
- (3) In accordance with Regulation 41 of the Uncertificated Securities Regulations 2001, the Company gives notice that only those shareholders entered on the relevant register of members (the "Register") for certificated or uncertificated shares of the Company (as the case may be) at 48 hours before the meeting time (the "Specified Time") will be entitled to attend or vote at the meeting in respect of the number of shares registered in their name at the time. Changes to entries on the Register after the Specified Time will be disregarded in determining the rights of any person to attend or vote at that meeting. Should the meeting be adjourned to a time not more than 48 hours after the Specified Time, that time will also apply for the purpose of determining the entitlement of members to attend and vote (and for the purpose of determining the number of votes they may cast) at the adjourned meeting. Should the meeting be adjourned for a longer period, then to be so entitled, members must be entered on the Register at the time which is 48 hours before the time fixed for the adjourned meeting or, if the Company gives notice of the adjourned meeting, at the time specified in the notice.
- (4) Copies of the Memorandum and Articles of Association, together with directors' service contracts or memoranda of the terms thereof (other than contracts expiring or determinable by the employing company without compensation within one year) and the register of interests of directors (and their families) in shares of the Company kept in accordance with Section 325 of the Companies Act 1985 will be available for inspection at the registered office of the Company during usual business hours on any weekday (Saturdays and public holidays excluded) from the date of this notice until the close of the Annual General Meeting and will be available for inspection at the place of the Annual General Meeting for at least fifteen minutes prior to and during the meeting.

FORM OF PROXY PIPEX Communications plc

I/We (see note (1) below) .....  
 BLOCK CAPITALS PLEASE

being (a) member(s) of the above-named Company, hereby appoint the Chairman of the Meeting or

(see note (2) below) as my/our proxy to attend and vote for me/us on my/our behalf at the Annual General Meeting of the Company to be held at the offices of Financial Dynamics, Holborn Gate, 26 Southampton Buildings, London WC2A 1PB on 7 June 2005 at 2pm and at any adjournment thereof.

In respect of the following Resolutions my proxy is instructed to vote as shown by "X" below.  
 (see note (3) below)

Ordinary Resolutions	For	Against	Abstain
Resolution 1 To receive the Report and Accounts			
Resolution 2 To re-elect Peter Dubens			
Resolution 3 To re-elect Laurence Blackall			
Resolution 4 To re-appoint KPMG Audit Plc			
Resolution 5 To authorise the directors to allot shares			
Special Resolutions			
Resolution 6 To disapply pre-emption rights			
Resolution 7 To authorise the Company to purchase its own shares			

Dated .....2005

Signature.....  
 (see note (4) below)

Name(s) .....  
 BLOCK CAPITALS PLEASE

Address: .....  
 (see note (5) below)

**Notes:**

- 1) In the case of joint shareholders all should be named but the signature of only the first named holder on the Register is required.
- 2) If any other proxy is preferred, please insert the name of the proxy desired in the space provided, delete the words "the Chairman of the Meeting" and initial the alteration. Such other proxy need not be a shareholder.
- 3) Please indicate with an "X" in the space provided how you wish your votes to be cast in respect of the Resolutions to be proposed. Unless expressly instructed otherwise in the form as to how the proxy is to vote on any particular matter, the proxy will vote or abstain at his/her discretion.
- 4) In the case of a corporation, this form of proxy must be under its Common Seal or under the hand of an officer or attorney duly authorised in writing. In the case of joint shareholders the signature of any one of them will suffice, but the names of joint holders should be stated.
- 5) To be valid this form of proxy and the Power of Attorney or other authority (if any) under which it is signed or a notarially certified copy thereof must be returned to the Company's Registrar, Capita Registrars, The Registry, 34 Beckenham Road, Beckenham, Kent BR3 4TU so as to arrive not later than 48 hours before the time appointed for the Meeting.



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BUSINESS REPLY SERVICE  
Licence No. MB122



Capita Registrars  
The Registry  
34 Beckenham Road  
Beckenham  
Kent BR3 4TU

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## ADVISORS

**Registered number**  
3974683

**Registered office**  
Carlton House  
27A Carlton Drive  
London  
SW15 2BS

**Auditors**  
KPMG Audit Plc  
8 Salisbury Square  
London  
EC4Y 8BB

**Stockbrokers**  
Collins Stewart Limited  
9th Floor  
88 Wood Street  
London  
EC2V 7QR

**Solicitors**  
SJ Berwin  
222 Gray's Inn Road  
London  
WC1X 8XF

Addleshaw Goddard  
25 Cannon Street  
London  
EC4M 5TB

**Registrar**  
Capita Registrars  
The Registry  
34 Beckenham Road  
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BR3 4TU

**Bankers**  
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