



NETWORK | CO-LOCATION | DEDICATED HOSTING

Quarterly Report  
December 31, 2006



**Peer 1 Network Enterprises, Inc.**  
**Consolidated Balance Sheet**  
**As At December 31, 2006**  
**(unaudited - prepared by management)**

	<b>December 2006 US\$</b>	<b>June 2006 US\$</b>
<b>Assets</b>		
<b>Current:</b>		
Cash and cash equivalents	4,834,125	5,666,477
Restricted Cash	505,000	505,000
Accounts receivable	3,553,878	5,241,027
Future income tax asset	357,488	-
Prepaid expenses	935,376	719,547
	<u>10,185,867</u>	<u>12,132,051</u>
<b>Other assets</b>	4,151,662	3,951,004
<b>Future income tax asset</b>	267,431	-
<b>Property, plant and equipment</b>	25,139,460	24,523,659
<b>Goodwill, licences and other intangibles</b>	6,770,616	7,676,380
	<u>46,515,036</u>	<u>48,283,094</u>
<b>Liabilities</b>		
<b>Current:</b>		
Accounts payable and accrued liabilities	5,973,816	10,038,981
Deferred revenue	3,988,613	3,748,932
Current portion of deferred gain	39,407	-
Current portion of deferred lease inducements	140,717	84,184
Current portion of notes payable	3,656,042	3,664,375
Income taxes payable	618,108	401,679
	<u>14,416,703</u>	<u>17,938,151</u>
<b>Deferred gain</b>	738,877	-
<b>Deferred lease inducements</b>	984,887	423,446
<b>Notes payable</b>	15,764,816	17,387,783
<b>Long Term Debt</b>	8,819,448	8,087,469
	<u>40,724,731</u>	<u>43,836,849</u>
<b>Shareholders' Equity</b>		
<b>Common Shares</b>	14,437,444	14,326,836
<b>Warrants</b>	1,060,865	1,060,865
<b>Contributed Surplus</b>	912,724	777,574
<b>Deficit</b>	(10,609,427)	(11,707,729)
<b>Cumulative Translation Adjustment</b>	(11,301)	(11,301)
	<u>5,790,305</u>	<u>4,446,245</u>
	<u>46,515,036</u>	<u>48,283,094</u>

APPROVED BY THE BOARD OF DIRECTORS:

\_\_\_\_\_  
 "Lance Tracey"

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 "David Harrison"

**Peer 1 Network Enterprises, Inc.**  
**Consolidated Income Statement**  
**Three and Six Months Ended December 31**  
**(unaudited - prepared by management)**

	Three Months Ended December 2006 US\$	Three Months Ended December 2005 US\$	Six Months Ended December 2006 US\$	Six Months Ended December 2005 US\$
Revenue	18,131,221	16,286,700	35,617,388	25,964,979
Cost of Sales	11,378,049	10,402,326	22,644,255	16,362,182
<b>Gross Profit</b>	<b>6,753,172</b>	<b>5,884,374</b>	<b>12,973,133</b>	<b>9,602,797</b>
Operating expenses	4,469,629	4,810,086	8,917,411	7,433,200
Operating Income before other items	2,283,543	1,074,288	4,055,722	2,169,597
Other Items:				
Amortization of preferred share discount	374,215	260,565	731,354	404,792
Interest expense - long term	835,663	1,041,378	1,661,489	2,033,875
Interest expense - short term	-	-	-	34,854
Interest accretion on notes payable	54,776	63,836	110,431	541,460
Integration costs	292,980	365,125	517,542	432,688
Foreign exchange loss (gain)	(4,882)	(174,993)	(37,769)	208,476
Loss on disposal of fixed assets	50,816	-	46,131	-
Loss from equity accounted investment	-	-	-	13,114
Income (Loss) before income taxes	679,975	(481,623)	1,026,544	(1,499,662)
Future income tax recovery	(624,919)	-	(624,919)	-
Current Income tax expense	456,043	-	553,161	-
Income tax recovery	(168,876)	-	(71,758)	-
Income (Loss) for the period	848,851	(481,623)	1,098,302	(1,499,662)
Deficit, beginning of period	(11,458,278)	(9,538,288)	(11,707,729)	(8,520,249)
Deficit, end of period	(10,609,427)	(10,019,911)	(10,609,427)	(10,019,911)
Basic earnings (loss) per share	0.01	(0.01)	0.01	(0.02)
Diluted earnings (loss) per share	0.01	(0.01)	0.01	(0.02)

**Peer 1 Network Enterprises, Inc.**  
**Consolidated Statement of Cash Flows**  
**Three and Six Months Ended December 31**  
**(unaudited - prepared by management)**

	Three Months Ended December 2006 US\$	Three Months Ended December 2005 US\$	Six Months Ended December 2006 US\$	Six Months Ended December 2005 US\$
<b>Cash flows from operating activities</b>				
Income (Loss) for the period	848,851	(481,624)	1,098,302	(1,499,662)
Amortization	2,671,387	2,347,620	5,277,151	3,788,496
Amortization of preferred share discount	374,215	260,565	731,354	404,792
Stock-based compensation included in income (loss) for period	111,475	154,139	166,223	179,704
Increase (decrease) in deferred lease inducements	(60,807)	101,203	617,974	162,344
Settlement of loan renewal fee	-	-	-	400,000
Bad debt expense	214,010	253,387	424,429	415,167
Loss on disposal of property and equipment	50,816	-	46,131	-
Amortization of deferred gain	(9,852)	-	(9,852)	-
Amortization of deferred loan origination fees	246,755	240,729	481,787	322,855
Future income tax recovery	(624,919)	-	(624,919)	-
Increase in accrued interest and accretion on notes payable	49,613	1,105,255	97,325	2,610,189
	<u>3,871,544</u>	<u>3,981,274</u>	<u>8,305,905</u>	<u>6,783,885</u>
Change in non-cash working capital items				
(Increase) decrease in accounts receivable	975,343	(606,095)	1,262,720	(2,210,717)
(Increase) decrease in prepaid expenses	(249,917)	435,502	(215,829)	(991,800)
Increase (decrease) in accounts payable and accrued liabilities	(1,473,801)	582,510	(4,931,660)	1,886,058
Increase (decrease) in income taxes payable	119,788	-	216,429	-
Increase in deferred revenue	310,808	151,695	239,681	1,956,546
	<u>3,553,765</u>	<u>4,544,886</u>	<u>4,877,246</u>	<u>7,423,972</u>
<b>Cash flows from investing activities</b>				
Acquisition of property and equipment	(2,468,530)	(2,172,232)	(4,621,497)	(15,804,605)
Investment in goodwill, licences and other intangibles	(203,301)	(249,917)	(527,995)	(3,577,463)
Proceeds on disposition of equipment	7,258	-	20,618	-
Investment in other assets	(625,062)	35,421	(682,445)	(2,891,432)
	<u>(3,289,635)</u>	<u>(2,386,728)</u>	<u>(5,811,319)</u>	<u>(22,273,500)</u>
<b>Cash flows from financing activities</b>				
Proceeds from (repayment of) notes payable and long term debt	(864,000)	(2,014,298)	(1,728,000)	22,550,344
Share capital issued	74,078	153,991	79,535	241,631
Net proceeds on sale leaseback	-	-	1,750,186	-
Repayment of shareholder notes	-	-	-	(2,249,629)
	<u>(789,922)</u>	<u>(1,860,307)</u>	<u>101,721</u>	<u>20,542,346</u>
Increase (Decrease) in cash and cash equivalents	(525,792)	297,851	(832,352)	5,692,818
Cash and cash equivalents - beginning of period	5,359,917	5,687,038	5,666,477	292,071
Cash and cash equivalents - end of period	<u>4,834,125</u>	<u>5,984,889</u>	<u>4,834,125</u>	<u>5,984,889</u>

## Notes to Unaudited Consolidated Financial Statements

### 1. Nature of Operations and Basis of Presentation:

Peer 1 Network Enterprises Inc. ("the Company") was incorporated under the laws of British Columbia. The Company is a provider of Internet infrastructure solutions and related managed services. Peer 1's service offerings include bandwidth, co-location and dedicated hosting services. Customers include hosting providers, online gaming companies, Internet phone (Voip) companies and small- and medium-sized businesses across North America. Peer 1 has established data centres and points of presence ("POPs") in 17 cities across North America and Europe including: Vancouver, Toronto, Montreal, New York, Seattle, San Jose, San Antonio, Los Angeles, Miami, Atlanta, Fremont, Herndon, Ashburn, Chicago, Dallas, Amsterdam and London, England.

The accompanying unaudited consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles for interim financial information and, accordingly do not include all information and note disclosures required for the annual financial statements under Canadian generally accepted accounting principles. It is management's opinion that all adjustments considered necessary for fair presentation of the financial position, results of operations and cash flow for the six month period have been made. These financial statements have been prepared in accordance with the same accounting principles applied in the preparation of the annual audited consolidated financial statements filed with the British Columbia Securities Commission for the fiscal year ended June 30, 2006. The annual financial statements should be referenced in conjunction with this interim report. Certain comparative amounts have been reclassified to correspond to the presentation in the current period.

### 2. Basis of Consolidation:

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Peer 1 Network (USA) Inc., Peer 1 Network (Seattle) Inc., Peer 1 Network (San Jose) Inc., Peer 1 Network (New York) Inc., Peer 1 Network (Nevada) GP, Inc., Peer 1 Network (Nevada) LP, Inc., ServerBeach Ltd., Data Center Technologies IP Inc., Peer 1 Dedicated Hosting Inc., Colobrokers.com Inc., 585065 B.C. Ltd., Peer 1 Network (Texas), LP and, Peer 1 Network (LA), Inc.

### 3. Share Capital

- a) Authorized :  
Unlimited Common shares without par value  
Unlimited Preferred shares without par value

- b) Issued and Fully Paid:

	<b>Number</b>	<b>Amount</b>
<b>Balance, June 30, 2006</b>	77,325,913	\$ 14,326,836
Stock Option Exercise	<u>16,000</u>	<u>8,349</u>

<b>Balance, September 30, 2006</b>	77,341,913	\$ 14,335,185
Stock Option Exercise	<u>200,000</u>	<u>102,259</u>
<b>Balance, December 31, 2006</b>	<u>77,541,913</u>	\$ <u>14,437,444</u>

c) Warrants Outstanding

The following non-transferable share purchase warrants are outstanding:

<i>Expiry Date</i>	<i>Exercise Price</i>	<i>Outstanding 6/30/2006</i>	<i>Issued</i>	<i>Expired/ Exercised</i>	<i>Outstanding 12/31/2006</i>
Jul 18, 2007	Cdn\$0.40	3,100,000	-	-	3,100,000
Sept 2, 2010	US\$0.23	2,306,571	-	-	2,306,571
Jan 31, 2011	Cdn\$0.40	833,333	-	-	833,333
		6,239,904	-	-	6,239,904

d) Contributed Surplus:

	<b>Amount</b>
<b>Balance, June 30, 2006</b>	\$ 777,574
Stock options exercised	(2,902)
Stock based compensation	<u>54,758</u>
<b>Balance, September 30, 2006</b>	829,430
Stock options exercised	(28,171)
Stock based compensation	<u>111,465</u>
<b>Balance, December 31, 2006</b>	\$ <u>912,724</u>

e) Shares held in escrow:

As of December 31, 2006, 7,365,601 shares of the company are subject to an escrow agreement and may not be transferred, assigned, or otherwise dealt with without the consent of the regulatory body that has jurisdiction.

f) Stock Options

The company has the following stock options outstanding:

<i>Expiry Date</i>	<i>Exercise Price</i>	<i>Outstanding 6/30/2006</i>	<i>Issued</i>	<i>Expired/ Exercised</i>	<i>Outstanding 12/31/2006</i>
May 30, 2011	Cdn\$0.75	75,000			75,000
April 3, 2011	Cdn\$0.65	465,000			465,000
Oct 26, 2011	Cdn\$0.64	-	800,000		800,000
Sept 6, 2011	Cdn\$0.63	-	2,973,100		2,973,100
Jan 16, 2011	Cdn\$0.59	200,000			200,000
Jan 31, 2011	Cdn\$0.55	40,000			40,000
Dec 1, 2010	Cdn\$0.47	500,000			500,000
Nov 30, 2010	Cdn\$0.47	10,000			10,000
May 30, 2009	Cdn\$0.46	15,000		5,000	10,000
July 24, 2007	Cdn\$0.45	2,128,250		100,000	2,028,250
Nov 7, 2007	Cdn\$0.45	300,000			300,000
June 30, 2009	Cdn\$0.45	15,000		5,000	10,000
Sept 30, 2010	Cdn\$0.45	2,500			2,500
March 8, 2009	Cdn\$0.44	300,000			300,000
Jan 29, 2009	Cdn\$0.42	10,000			10,000
Oct 6, 2010	Cdn\$0.41	100,000			100,000
Oct 31, 2010	Cdn\$0.40	2,500			2,500
Nov 7, 2007	Cdn\$0.39	100,000			100,000
July 29, 2010	Cdn\$0.39	110,000		100,000	10,000
Oct 20, 2009	Cdn\$0.38	175,000		5,000	170,000
Aug 31, 2010	Cdn\$0.36	7,500			7,500
May 31, 2010	Cdn\$0.35	35,000			35,000
Sept 9, 2008	Cdn\$0.32	332,000		11,000	321,000
Sept 30, 2009	Cdn\$0.31	5,000			5,000
Mar 1, 2010	Cdn\$0.30	30,000			30,000
Feb 28, 2010	Cdn\$0.30	10,000			10,000
Apr 30, 2010	Cdn\$0.30	20,000		10,000	10,000
Nov 30, 2009	Cdn\$0.28	12,000			12,000
Dec 31, 2009	Cdn\$0.28	10,000		5,000	5,000
Jan 31, 2010	Cdn\$0.24	15,000			15,000
		5,024,750	3,773,100	241,000	8,556,850

4. Related Party Transactions

The Company has entered into a number of related party transactions with companies either owned or subject to significant influence by management, directors and principal shareholders.

The significant transactions with related parties for the six month period ended December 31 are as follows:

	<b>FY2007</b>	<b>FY2006</b>
Revenue earned	\$60,188	\$56,563
Interest expensed	-	\$334,286
Other expenses	\$264,608	\$8,902

These transactions are in the normal course of operations and are measured at their exchange amounts, which is the amount of consideration established and agreed to by the related parties. Included in other expenses is \$11,869 (\$139 in 2006) in accounts receivable that has been written off.

	FY2007	FY2006
<hr/>		
Balances at December 31 -		
Accounts receivable from related companies	\$7,934	\$91,208
Accounts payable to a related party	\$9,248	\$525

The balances are payable on demand and have arisen from the sale of products and provision of services referred to above.

## 5. Segmented Information

Following the acquisition of ServerBeach assets on October 20, 2004 and commencement of the provision of dedicated servers, two reporting segments are now in operation.

	<i>Three months ended December 31, 2006</i>			<i>Three months ended December 31, 2005</i>		
	<i>Colocation &amp; Bandwidth</i>	<i>Dedicated Servers</i>	<i>Total</i>	<i>Colocation &amp; Bandwidth</i>	<i>Dedicated Servers</i>	<i>Total</i>
Revenue	\$5,102,055	\$13,029,166	\$18,131,221	\$4,450,152	\$11,836,548	\$16,286,700
Income (loss)	\$(235,376)	\$1,084,227	\$848,551	\$(1,911,525)	\$1,429,902	\$ (481,623)

  

	<i>Six months ended December 31, 2006</i>			<i>Six months ended December 31, 2005</i>		
	<i>Colocation &amp; Bandwidth</i>	<i>Dedicated Servers</i>	<i>Total</i>	<i>Colocation &amp; Bandwidth</i>	<i>Dedicated Servers</i>	<i>Total</i>
Revenue	\$10,099,488	\$25,517,900	\$35,617,388	\$8,550,512	\$17,414,467	\$25,964,979
Income (loss)	\$(865,623)	\$1,963,925	\$1,098,302	\$(3,083,490)	\$1,583,828	\$ (1,499,662)
Total Assets	\$17,155,087	\$29,359,949	\$46,515,036	\$16,961,176	\$30,142,339	\$ 47,103,515

## Segmented Information (continued)

The Company operates in two geographic segments, USA and Canada.

	<i>Three months ended December 31, 2006</i>			<i>Three months ended December 31, 2005</i>		
	<i>USA</i>	<i>Canada</i>	<i>Total</i>	<i>USA</i>	<i>Canada</i>	<i>Total</i>
Revenue	\$14,298,735	\$ 3,832,486	\$18,131,221	\$12,816,063	\$3,470,637	\$16,286,700
Income (loss)	\$(116,772)	\$965,623	\$848,851	\$(1,870,563)	\$1,388,940	\$(481,623)

	<i>Six months ended December 31, 2006</i>			<i>Six months ended December 31, 2005</i>		
	<i>USA</i>	<i>Canada</i>	<i>Total</i>	<i>USA</i>	<i>Canada</i>	<i>Total</i>
Revenue	\$28,064,912	\$ 7,552,476	\$35,617,388	\$19,411,618	\$6,553,361	\$25,964,979
Income (loss)	\$(395,163)	\$1,493,465	\$1,098,302	\$(2,238,798)	\$739,136	\$(1,499,662)
Total Assets	\$35,461,521	\$11,053,515	\$46,515,036	\$36,976,259	\$10,127,256	\$ 47,103,515