

Edgar Filing: RAPID LINK INC - Form 10QSB

RAPID LINK INC  
Form 10QSB  
June 14, 2006

United States  
Securities and Exchange Commission  
Washington, D.C. 20549

FORM 10-QSB

(Mark One)

Quarterly Report under Section 13 or 15(d) of the Securities  
Exchange Act of 1934

For the quarterly period ended April 30, 2006  
-----

Or

Transition Report under Section 13 or 15(d) of the Exchange Act

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-22636  
-----

RAPID LINK, INCORPORATED

-----  
(Exact name of small business issuer as specified in its charter)

Delaware

75-2461665

-----  
(State or other jurisdiction of  
incorporation or organization)

-----  
(I.R.S. Employer  
Identification No.)

17383 Sunset Boulevard, Suite 350  
Los Angeles, California, 90272

-----  
(Address of principal executive offices)

-----  
(Zip Code)

(310) 566-1700

-----  
(Issuer's Telephone number)

N/A

-----  
(Former name, former address and former fiscal year,  
if changed since last report)

Check whether the issuer (1) filed all reports required to be filed by  
Section 13 or 15(d) of the Exchange Act during the past 12 months (or for  
such shorter period that the registrant was required to file such reports),  
and (2) has been subject to such filing requirements for the past 90 days.  
Yes  No

Indicate by checkmark whether the registrant is a shell company (as defined  
in Rule 12b-2 of the Exchange Act). Yes  No

As of June 14, 2006, 30,386,794 shares of common stock, \$.001 par value per  
share, were outstanding.

Transitional small business disclosure format (Check One): Yes  No

# Edgar Filing: RAPID LINK INC - Form 10QSB

## PART I - FINANCIAL INFORMATION

### Item 1. Financial Statements

#### RAPID LINK INCORPORATED AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS

ASSETS -----	April 30, 2006	October 31, 2005
	-----	-----
	(unaudited)	
<b>CURRENT ASSETS</b>		
Cash and cash equivalents	\$ 167,841	\$ 172,164
Trade accounts receivable, net of allowance for doubtful accounts of \$452,109 at April 30, 2006 and \$427,099 at October 31, 2005	703,820	564,039
Prepaid expenses and other current assets	100,179	164,978
	-----	-----
Total current assets	971,840	901,181
	-----	-----
PROPERTY AND EQUIPMENT, net	225,138	353,726
GOODWILL, net	1,796,917	1,796,917
OTHER ASSETS, net	327,916	219,043
	-----	-----
<b>TOTAL ASSETS</b>	<b>\$ 3,321,811</b>	<b>\$ 3,270,867</b>
	=====	=====
 <b>LIABILITIES AND SHAREHOLDERS' DEFICIT</b> -----		
<b>CURRENT LIABILITIES</b>		
Capital lease obligation	126,196	126,196
Trade accounts payable	3,462,734	3,451,801
Accrued liabilities	795,077	887,975
Accrued interest (including \$952,019 to related parties at April 30, 2006 and \$901,849 at October 31, 2005)	1,150,454	1,007,322
Deferred revenue	427,636	401,640
Deposits and other payables	418,109	418,109
Convertible debentures, current portion, net of debt discount of \$1,038,067 at April 30, 2006 and \$223,167 at October 31, 2005	1,169,391	481,833
Net current liabilities from discontinued operations	1,162,000	1,162,000
	-----	-----
Total current liabilities	8,711,597	7,936,876
	-----	-----
CONVERTIBLE DEBENTURES, net of current portion and net of debt discount of \$833,333 at April 30, 2006 and \$1,140,824 at October 31, 2005	416,667	686,633
CONVERTIBLE NOTES PAYABLE TO RELATED PARTIES, net of debt discount of \$60,664 at January 31, 2006 and \$77,208 at October 31, 2005	942,726	926,182

## Edgar Filing: RAPID LINK INC - Form 10QSB

### COMMITMENTS AND CONTINGENCIES

#### SHAREHOLDERS' DEFICIT

Preferred stock, \$.001 par value; 10,000,000 shares authorized; none issued and outstanding	-	-	
Common stock, \$.001 par value; 175,000,000 shares authorized; 30,398,816 shares issued at April 30, 2006 and 29,297,183 at October 31, 2005	30,400	29,298	
Additional paid-in capital	43,938,910	42,858,862	
Accumulated deficit	(50,663,619)	(49,112,114)	
Treasury stock, 12,022 common shares at cost	(54,870)	(54,870)	
	-----	-----	
Total shareholders' deficit	(6,749,179)	(6,278,824)	
	-----	-----	
TOTAL LIABILITIES AND SHAREHOLDERS' DEFICIT	\$ 3,321,811	\$ 3,270,867	
	=====	=====	

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

### RAPID LINK INCORPORATED AND SUBSIDIARIES UNAUDITED INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS

	Three Months Ended April 30,		Six Months Ended April 30,	
	2006	2005	2006	2005
	-----	-----	-----	-----
REVENUES	\$ 2,121,018	\$ 2,864,960	\$ 4,107,130	\$ 5,649,212
COSTS AND EXPENSES				
Costs of revenues	1,612,960	2,385,165	3,141,075	4,382,579
Sales and marketing	99,827	42,919	242,209	97,528
General and administrative	732,995	849,937	1,390,419	1,600,018
Depreciation and amortization	99,967	150,415	204,179	296,649
(Gain) Loss on disposal of property and equipment	34,229	-	34,229	(8,800)
	-----	-----	-----	-----
Total costs and expenses	2,579,978	3,428,436	5,012,111	6,367,974
	-----	-----	-----	-----
Operating loss	(458,960)	(563,476)	(904,981)	(718,762)
OTHER INCOME (EXPENSE)				
Interest expense and financing costs	(355,370)	(54,092)	(603,751)	(108,181)
Related party interest expense and financing costs	(33,357)	(36,772)	(66,414)	(73,544)
Foreign currency exchange gains (loss)	1,358	(2,788)	23,641	7,359
	-----	-----	-----	-----
Total other income (expense), net	(387,369)	(93,652)	(646,524)	(174,366)
	-----	-----	-----	-----
NET LOSS	\$ (846,329)	\$ (657,128)	\$ (1,551,505)	\$ (893,128)
	=====	=====	=====	=====
NET LOSS PER COMMON SHARE:				
Basic and diluted net loss per share	\$ (0.03)	\$ (0.03)	\$ (0.05)	\$ (0.04)
	=====	=====	=====	=====

## Edgar Filing: RAPID LINK INC - Form 10QSB

WEIGHTED AVERAGE COMMON SHARES USED IN  
THE CALCULATION OF PER SHARE AMOUNTS:

Basic and diluted	30,237,903	23,022,129	29,759,747	23,022,129
	=====	=====	=====	=====

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

### RAPID LINK INCORPORATED AND SUBSIDIARIES UNAUDITED INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS

	Six Months Ended April 30,	
	2006	2005
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net loss	\$ (1,551,505)	\$ (893,128)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
(Gain) loss from disposal of property and equipment	34,229	(8,800)
Bad debt expense	(25,010)	(21,000)
Non-cash interest expense	510,126	-
Depreciation and amortization	204,179	296,649
Warrants issued for legal services	-	159,695
(Increase) decrease in:		
Trade accounts receivable	(114,771)	(125,969)
Prepaid expenses and other current assets	(35,201)	(19,703)
Other assets	(1,784)	(1,388)
Increase (decrease) in:		
Trade accounts payable	10,933	634,448
Accrued liabilities	56,384	21,015
Deferred revenue	25,996	(8,286)
Deposits and other payables	-	(10,000)
	(886,424)	23,533
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Purchase of property and equipment	(73,749)	(22,561)
Proceeds from sale of property and equipment	-	10,000
	(73,749)	(12,561)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from convertible debenture	1,000,000	-
Payment of financing fees	(44,150)	-
Proceeds from shareholder advance	500,000	-
Payment of shareholder advance	(500,000)	-
	955,850	-
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<b>(4,323)</b>	<b>10,972</b>
Cash and cash equivalents at beginning of period	172,164	586,389
Cash and cash equivalents at end of period	\$ 167,841	\$ 597,361

## Edgar Filing: RAPID LINK INC - Form 10QSB

### SUPPLEMENTAL SCHEDULE OF NON CASH INVESTING AND FINANCING ACTIVITIES

Conversion of debt to common stock	\$	75,000	\$	-
Conversion of Accrued interest into common stock		6,150		-
Fair market value of warrants issued with debt		327,176		-
Beneficial conversion feature recorded in connection with debt issuances		628,674		-

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

### RAPID LINK INCORPORATED AND SUBSIDIARIES

#### NOTES TO UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

##### NOTE 1 - OPERATIONS AND BASIS OF PRESENTATION

The consolidated financial statements of Rapid Link, Incorporated and its subsidiaries, "Rapid Link" or "the Company", included in this Form 10-QSB are unaudited and do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the financial position and operating results for the three and six month periods ended April 30, 2006 and 2005 have been included. Operating results for the three and six month periods ended April 30, 2006 are not necessarily indicative of the results that may be expected for the fiscal year ending October 31, 2006. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's annual report on Form 10-KSB for the fiscal year ended October 31, 2005.

Rapid Link has served as a facilities-based, global Internet Protocol ("IP") communications company providing connectivity to international markets experiencing significant demand for IP enabled services. Rapid Link provides a variety of international telecommunications services targeted to small and medium sized enterprises ("SME's") and niche markets, such as the United States Military and Armed Forces that include the transmission of voice and data traffic and the provision of Web-based and other communications services. Rapid Link utilizes Voice over Internet Protocol ("VoIP") packetized voice technology to improve both cost and efficiencies of telecommunication transmissions. Rapid Link utilizes the Internet to transport the Company's communications.

Beginning in the fourth quarter of fiscal 2004, the Company shifted its retail product focus to value-added VoIP communication services to customers, both domestically and internationally, although to date the Company has not derived significant revenues from this new offering. Rapid Link focuses on the US military and other key niche markets. The Company offers PC-to-PC, PC-to-phone, and phone-to-phone calling on their set of Internet Access Device's ("IAD's") that provide a low cost phone service that is delivered through a broadband connection. Rapid Link offers VoIP service plans to residential and business customers in addition to serving the military. The Company's flat rate service plans provide unlimited calling within the United States and Canada. These plans include free features such as voice mail, call forwarding, three way calling and other features as a part of the service. Rapid Link's VoIP IAD's for consumers and businesses consists of single and multi-line routers, which enables customers to convert their traditional phone into a VoIP phone, or a headset

## Edgar Filing: RAPID LINK INC - Form 10QSB

that plugs directly into the customer's computer so that it can be used as a phone as the customer travels. All of the services connect through the Internet. The customer can then make and receive calls through their unique phone number using VoIP.

### Estimates and Assumptions

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

### NOTE 2 - GOING CONCERN

The Company is subject to various risks in connection with the operation of its business including, among other things, (i) changes in external competitive market factors, (ii) inability to satisfy anticipated working capital or other cash requirements, (iii) changes in the availability of transmission facilities, (iv) changes in the Company's business strategy or an inability to execute its strategy due to unanticipated changes in the market, (v) various competitive factors that may prevent the Company from competing successfully in the marketplace, and (vi) the Company's lack of liquidity and its ability to raise additional capital. As of April 30, 2006 the Company has an accumulated deficit of approximately \$50.7 million as well as a working capital deficit of approximately \$7.7 million. In addition, approximately 74% of the Company's trade accounts payable and accrued liabilities are past due. Funding of the Company's working capital deficit, its current and future anticipated operating losses, and growth of the Company's retail revenues will require continuing capital investment. Historically, the Company has received significant funding from a major shareholder. The Company's strategy is to fund these cash requirements through debt facilities and additional equity financing.

Although the Company has been able to arrange debt facilities and equity financing to date, there can be no assurance that sufficient debt or equity financing will continue to be available in the future or that it will be available on terms acceptable to the Company. Failure to obtain sufficient capital would materially affect the Company's operations in the short term and expansion strategies. The Company will continue to explore external financing opportunities and renegotiation of its short-term debt with its current financing partners in order to extend the terms or retire these obligations. Currently, the Company is in negotiations with multiple parties to obtain additional financing, and the Company will continue to explore financing opportunities with additional parties. At April 30, 2006, approximately 22% of the gross debt is due to the senior management and a Director of the Company.

As a result of the aforementioned factors and related uncertainties, there is substantial doubt about the Company's ability to continue as a going concern. The consolidated financial statements do not include any adjustments to reflect the possible effects of recoverability and classification of assets or classification of liabilities, which may result from the inability of the Company to continue as a going concern.

### NOTE 3 - CONCENTRATION OF CREDIT RISK AND SIGNIFICANT CUSTOMERS

The Company provided wholesale services to one customer who accounted for 13% of the overall revenue of the Company for the three months ended April 30, 2006 and 13% of the Company's trade accounts receivable at April 30, 2006. The Company provided wholesale services to one customer who accounted

## Edgar Filing: RAPID LINK INC - Form 10QSB

for 16% of the overall revenue of the Company for the six months ended April 30, 2006. For the three months ended April 30, 2006, two of the Company's suppliers accounted for approximately 17% and 10%, respectively, of the Company's total costs of revenues.

The Company provided wholesale services to two customers, each of which accounted for 13% of the overall revenue of the Company for the three months ended April 30, 2005. No customers accounted for more than 10% of sales during the six months ended April 30, 2005. The Company provided wholesale services to another customer which accounted for 15% of the Company's trade accounts receivable at April 30, 2005. For the three months ended April 30, 2005, one of the Company's suppliers accounted for approximately 21% of the Company's total costs of revenues.

### NOTE 4 - STOCK-BASED COMPENSATION

The Company accounts for stock-based employee compensation arrangements in accordance with provisions of Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," and complies with the disclosure provisions of SFAS No. 123, "Accounting for Stock-Based Compensation," as amended by SFAS No. 148 "Accounting for Stock-Based Compensation - Transition and Disclosure". Under APB Opinion No. 25, compensation expense for employees is based on the excess, if any, on the date of grant, of fair value of the Company's stock over the exercise price. Accordingly, no compensation cost has been recognized for its employee stock options in the financial statements during the three months ended April 30, 2006 and April 30, 2005 as the fair market value on the grant date approximates the exercise price. Had the Company determined compensation cost based on the fair value at the grant date for its stock options under SFAS No.123, as amended by SFAS No. 148, the Company's pro forma net loss for the three months ended April 30, 2006 and 2005 would have been as follows:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2006	2005	2006	2005
Net loss	\$ (846,329)	\$ (657,128)	\$ (1,551,505)	\$ (893,128)
Deduct: Stock based employee compensation expense determined under fair value based method	(2,696)	(3,554)	(5,444)	(7,188)
Pro forma net loss	\$ (849,025)	\$ (660,682)	\$ (1,556,949)	\$ (900,316)
Net loss per share				
As reported				
Basic and diluted	\$ (0.03)	\$ (0.03)	\$ (0.05)	\$ (0.04)
Proforma				
Basic and diluted	\$ (0.03)	\$ (0.03)	\$ (0.05)	\$ (0.04)

For purposes of pro forma disclosures, the estimated fair value of the options is amortized to expense over the options' vesting periods. Because options vest over a period of several years and additional awards are

## Edgar Filing: RAPID LINK INC - Form 10QSB

generally made each year, the pro forma information presented above is not necessarily indicative of the effects on reported or pro forma net earnings or losses for future periods.

No options were granted during the six months ended April 30, 2006 and 2005.

In December 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 123 (revised 2004) ("Statement 123(R)"), "Share-Based Payment", which revised SFAS No. 123 and supercedes APB Opinion No. 25. The revised statement addresses the accounting for share-based payment transactions with employees and other third parties, eliminates the ability to account for share-based compensation transactions with employees using APB Opinion No. 25 and requires that the fair value of such share-based payments be recognized in the consolidated statement of operations. The revised statement is effective as of the first annual financial reporting period beginning after December 15, 2005. The Company will adopt the statement on November 1, 2006 as required. The impact of adoption of Statement 123(R) cannot be predicted at this time because it will depend on levels of share-based payments granted in the future. However, had the Company adopted Statement 123(R) in prior periods, the impact of that standard would have approximated the impact of SFAS No. 123 as described in the disclosure of pro forma net loss and net loss per share above.

### NOTE 5 - RESOLUTION OF VENDOR DISPUTE

During the first quarter of fiscal year 2005, the Company recorded a reduction of \$283,138 to Costs of Revenues in its Consolidated Statement of Operations. This amount represents the favorable resolution of a dispute with one of the Company's vendors. This amount had been recorded as Costs of Revenues in prior periods.

### NOTE 6 - CONVERTIBLE DEBENTURES AND CONVERTIBLE NOTES PAYABLE TO RELATED PARTIES

On June 1, 2005, the Company and GCA Strategic Investment Fund ("GCA") agreed to extend the maturity dates of the Company's two 6% convertible debentures, each convertible debenture providing financing of \$550,000 in January 2002 and July 2003, respectively. For the convertible debenture originally issued in January 2002, the maturity date was extended to November 26, 2006. The gross balance of this debenture was \$430,000 at April 30, 2006. In connection with the extension, the Company issued GCA warrants to acquire 110,000 shares of common stock at an exercise price of \$0.11 and warrants to acquire 150,000 shares of our common stock at an exercise price of \$0.38. Both warrants expire in June 2010. The Company recorded \$104,693 as debt discount, representing the relative fair value of the warrants on June 1, 2005. This amount was calculated using the Black-Scholes pricing model with the following assumptions: applicable risk-free interest rate based on the current treasury-bill interest rate at the grant date of 4%; dividend yields of 0%; volatility factors of the expected market price of the Company's common stock of 1.64; and an expected life of the warrants of three years. The debt discount was amortized over the extension period of the convertible debenture and is fully amortized at April 30, 2006. In addition, the Company issued to GCA 100,000 shares of common stock valued at \$0.45 per share, the Company's closing stock price on June 1, 2005, the date of issuance. In connection with the stock issuance, the Company recorded \$45,000 as debt discount, and amortized the debt discount over the extension period of the convertible debenture which ended in the first quarter of 2006. For the convertible debenture originally issued in July 2003, the maturity date was extended to November 26, 2006. The gross



## Edgar Filing: RAPID LINK INC - Form 10QSB

balance of this debenture was approximately \$550,000 at April 30, 2006. In connection with the extension, the Company issued GCA warrants to acquire 150,000 shares of common stock at an exercise price of \$0.38, which expire in June 2010. The Company recorded \$58,458 as debt discount, representing the fair value of the warrants on June 1, 2005. This amount was calculated using the Black-Scholes pricing model with the following assumptions: applicable risk-free interest rate based on the current treasury-bill interest rate at the grant date of 4%; dividend yields of 0%; volatility factors of the expected market price of the Company's common stock of 1.64; and an expected life of the warrants of three years. The debt discount is being amortized over the extension period of the convertible debenture. In addition, the Company issued to GCA 40,000 shares of common stock valued at \$0.45 per share, the Company's closing stock price on June 1, 2005, the date of issuance. In connection with the stock issuance, the Company recorded \$18,000 as debt discount and is amortizing the debt discount over the extension period of the convertible debenture. For the six months ended April 30, 2006, approximately \$25,000 of deferred financing fees and debt discount amortization has been recorded as interest expense. The remaining unamortized discount is \$29,733 at April 30, 2006.

During fiscal 2005, GCA elected to convert \$35,000 of the gross principal balance of the January 2002 convertible debenture into approximately 352,000 shares of common stock. During fiscal year 2006, GCA elected to convert \$25,000 of the gross principal balance of the January 2002 convertible debenture into approximately 407,000 shares of common stock. There were no other conversions during the quarter ended April 30, 2006. On March 8, 2006, the Company and GCA Strategic Investment Fund ("GCA") agreed to extend the maturity date of the Company's 6% convertible debenture, which originally provided providing financing of \$550,000 in January 2002 (GCA-Debenture). The maturity date for the GCA-Debenture was extended to November 26, 2006.

On June 1, 2005, the Company and Global Capital Funding Group, LP ("Global") agreed to extend the maturity date of the Company's 12% note payable (the "GC-Note"), which provided financing of \$1,250,000 in November 2002. The maturity date was extended to February 29, 2008. In connection with the extension, the GC-Note was converted to a 10.08% Convertible Note ("GC-Conote"). The conversion price is equal to 80% of the average of the three lowest volume weighted average sales prices as reported by Bloomberg L.P. during the twenty Trading Days immediately preceding the related Notice of Conversion (the "Formula Conversion Price"). The Company calculated the beneficial conversion feature embedded in the GC-Conote in accordance with EITF 98-5 "Accounting for Convertible Securities with Beneficial Conversion Features or Contingently Adjustable Conversion Ratios" ("EITF-98-5") and EITF 00-27 "Application of Issue No. 98-5 to Certain Convertible Instruments" ("EITF 00-27") and recorded \$1,013,032 as debt discount. This debt discount is being amortized over the life of the GC-Conote. The Company also issued to the holder of the GC-Conote warrants to acquire an aggregate of 500,000 shares of common stock at an exercise price of \$0.38, and 125,000 warrants to purchase common stock at \$0.11 per share, both warrants expiring in June 2010. The Company recorded \$200,498 as debt discount, the relative fair value of the warrants on June 1, 2005. This amount was calculated using the Black-Scholes pricing model with the following assumptions: applicable risk-free interest rate based on the current treasury-bill interest rate at the grant date of 4%; dividend yields of 0%; volatility factors of the expected market price of the Company's common stock of 1.64; and an expected life of the warrants of three years. The debt discount is being amortized over the life of the GC-Conote. In addition, the Company issued to Global 100,000 shares of common stock valued at \$0.45 per share, the Company's closing stock price on June 1, 2005, the date of issuance. The Company recorded \$36,469 as debt discount, the relative fair value of the stock issued, and is amortizing the debt discount over the life of the GC-Conote. For the six months ended

## Edgar Filing: RAPID LINK INC - Form 10QSB

April 30, 2006, approximately \$227,000 of debt discount amortization has been recorded as interest expense. The remaining unamortized discount is \$833,333 at April 30, 2006.

In connection with the extension of the maturity date of the GC-Note, the interest due on the GC-Note of approximately \$350,000 as of May 31, 2005 was converted to a \$400,000 non-interest bearing convertible Note Payable (the "GC-Note2) to Global Capital Funding Group, LP. The GC-Conote2 requires quarterly payments of \$50,000 on the last day of March, June, September and December of each year until the March 31, 2007 maturity Date, commencing on June 30, 2005. In addition, the GC-Conote2 provides for conversion based on a conversion price equal to 80% of the average of the three lowest volume weighted average sales prices as reported by Bloomberg L.P. during the twenty Trading Days immediately preceding the related Notice of Conversion (the "Formula Conversion Price"). The Company calculated the beneficial conversion feature embedded in the GC-Note2 in accordance with EITF 98-5 and recorded approximately \$350,000 as debt discount. This debt discount is being amortized over the life of the GC-Note2. The approximate \$50,000 difference between the accrued interest at May 31, 2005 and the value of the GC-Note2 represents a financing fee and was recorded as debt discount and is being amortized over the life of the GC-Note2. For the six months ended April 30, 2006, \$50,000 of debt discount amortization has been recorded as interest expense. The gross balance of the GC-Note2 was \$225,000 at April 30, 2006. The remaining unamortized discount was \$175,000 at April 30, 2006.

During fiscal year 2005, GCA elected to convert \$75,000 of the GC-Note2 into approximately 657,000 shares of common stock. During fiscal year 2006 GCA elected to convert \$50,000 of the GC-Note2 into approximately 694,000 shares of common stock. Although the Company has not made its scheduled September and December 2005 payments, and March 2006 payment, Global has not declared the note to be in default, and continues to convert the balance into shares of common stock.

On July 21, 2005, the Company and the three executives that hold a 10% convertible debenture (the "Notes") agreed to extend the maturity date of the Notes to February 29, 2008. The original maturity date was October 24, 2003. In connection with the extension, the Company issued to the three executives warrants to acquire 640,000 shares of common stock at an exercise price of \$0.16. The warrants expire in July 2010. The Company recorded \$88,238 as debt discount, the fair value of the warrants. This amount was calculated using the Black-Scholes pricing model with the following assumptions: applicable risk-free interest rate based on the current treasury-bill interest rate at the grant date of 4%; dividend yields of 0%; volatility factors of the expected market price of the Company's common stock of 1.65; and an expected life of the warrants of three years. The debt discount is being amortized over the extension period of the Notes. For the six months ended April 30, 2006, approximately \$17,000 of debt discount amortization has been recorded as interest expense. The gross balance of the Notes was \$1,003,390 at April 30, 2006. The remaining unamortized discount was \$60,664 at April 30, 2006.

On March 8, 2006, the Company completed a private placement of two one year 10% convertible debentures ("Debentures"), for gross proceeds of \$1,000,000. In connection with the Debentures, the Company agreed to issue the investors a total of 2,000,000 immediately exercisable five year warrants to purchase the Company's common stock at an exercise price of \$0.14 for 1,000,000 warrants, and \$0.25 for an additional 1,000,000 warrants. The Company paid \$44,150 in financing fees in connection with the Debentures which were recorded as financing fees. Additionally in connection with these Debentures the Company recorded a debt discount of \$1,000,000 related to the fair value of warrants issued and the related beneficial conversion feature that will be amortized over the life of the loan. This amount was calculated using the

## Edgar Filing: RAPID LINK INC - Form 10QSB

Black-Scholes pricing model with the following assumptions: applicable risk-free interest rate based on the current treasury-bill interest rate at the grant date of 4.77%; dividend yields of 0%; volatility factors of the expected market price of the Company's common stock of 0.25; and an expected life of the warrants of three years. During the three-months ended April 30, 2006 the Company recorded expense of \$167,000 in relation to the amortization of these fees. The remaining unamortized debt discount totaled \$833,333 at April 30, 2006.

### NOTE 7 - ADVANCES FROM SHAREHOLDER

During the three months ended January 31, 2006, the Company's chief executive officer, and significant shareholder, John Jenkins, advanced funds to the Company in the aggregate amount of \$500,000. During the three-month period ended April 30, 2006 the Company has re-paid this amount in full with proceeds received from the Debentures.

### NOTE 8 - DISCONTINUED OPERATIONS

During the first quarter of fiscal year 2004, the Company determined based on final written communications with the State of Texas that the Company had a liability for sales taxes (including penalties and interest) totaling \$1.1 million. The Company had previously accrued an estimated settlement amount of \$350,000 during fiscal year 2003. During the first quarter of fiscal year 2004, the Company accrued an additional \$750,000. On August 5, 2005, the State of Texas filed a lawsuit in the 53rd Judicial District Court of Travis County, Austin, Texas against the Company. The lawsuit requests payment of approximately \$1.162 million including penalties and interest for state and local sales tax. During the fiscal year 2005, the Company accrued an additional \$62,000 in amounts due. The sales tax amount due is attributable to audit findings of the State of Texas for the years 1995 to 1999 associated with Canmax Retail Systems, a current subsidiary of ours, and former operating subsidiary providing retail automation software and related services to the retail petroleum and convenience store industries. The State of Texas determined that Canmax Retail Systems did not properly remit sales tax on certain transactions. Management believes that it will be able to negotiate a reduced settlement amount with the state, although there can be no assurance that the Company will be successful with respect to such negotiations. These operations were previously classified as discontinued after the Company sold its retail automation software business in December 1998 and changed its business model to international wholesale and retail business, operating as a facilities-based global Internet protocol communications company providing connectivity to international markets. Since this sales tax liability represents an adjustment to amounts previously reported in discontinued operations, the amount was classified as Discontinued Operations. The amount that the State of Texas assessed of \$1.162 million has been accrued as a liability and is included in the April 30, 2006 Balance Sheet as discontinued operations.

### NOTE 9 - SUBSEQUENT EVENTS

On May 5, 2006, Rapid Link, Incorporated entered into a definitive stock purchase agreement (the "Purchase Agreement") to acquire from Apex Acquisitions, Inc. (the "Stockholder"), all of the issued and outstanding shares of capital stock of Telenational Communications, Inc., a privately owned Delaware corporation ("Telenational") that is a provider of domestic and international long distance services, including internationally originated direct access calling services and pre-paid and post-paid calling card services. The total purchase price for this acquisition is \$4.76

## Edgar Filing: RAPID LINK INC - Form 10QSB

million. Pursuant to the terms of the Purchase Agreement, in consideration for the acquisition of all of the issued and outstanding shares of Telenational (the "Telenational Shares"), the Company has agreed to deliver a \$1 million note payable, due and payable on the 18-month anniversary of closing which bears interest at the rate of 8% per annum. The note is secured by all of the outstanding shares of the Telenational stock. Additionally the Company issued 9,587,500 shares of its common stock (the "Initial Stock Payment") as contemplated by the Purchase Agreement (the "Closing"). If Telenational's monthly retail and wholesale gross margin combined (the "Average Monthly Gross Profit") averages at least \$300,000 per month ("Target Average Gross Margin") for the calendar year ended December 31, 2005, then the Stockholder shall be entitled to all of the Initial Stock Payment. If the Fiscal 2005 Average Monthly Gross Profit is less than the Target Average Gross Margin, the Initial Stock Payment will be reduced proportionately. In the event that Telenational's First Aggregate Monthly Gross Profit is less than \$900,000 (the "Target Aggregate Monthly Gross Profit"), then the Contingent Stock Payment shall be reduced by a number of shares to be determined by taking the product obtained by multiplying \$750,000 by a fraction whose numerator is the Target Aggregate Monthly Gross Profit less the First Aggregate Monthly Gross Profit and whose denominator is the Target Aggregate Monthly Gross Profit; and divided by the volume weighted average closing price per share of our common stock as reported on the Over-the-Counter Bulletin Board (or any other securities exchange or inter-dealer quotation system on which our common stock is then listed) for the 15 consecutive trading days ending on the day prior to the first anniversary of the Closing (the "Per Share Price"); provided, however, that such Per Share Price shall be not less than \$0.13 per share and not greater than \$0.25 per share. Subject to adjustment based on any shortfall as determined in accordance with above. The purchase price (adjusted downward for this calculation by 25%) will be proportionately reduced by the percentage shortfall of the actual gross margin achieved against the Target Gross Margin. Any reduction in the adjusted purchase price will be applied against the stock portion of the purchase price. Further, the "earn out" shares in the amount of 9,587,500 additional shares that were to be issued following the 12-month anniversary of the Closing (the "Contingent Stock Payment") based on Telenational maintaining a \$300,000 gross monthly margin for that 12 month period was deemed earned and delivered to Apex Acquisitions, Inc. by the Board of Directors on June 5, 2006, so that the integration of the two company's would not be delayed in the best interest of the company.

At the closing date of this acquisition, the shareholders of Telenational will provide a working capital loan to the Company in the amount of a minimum of \$200,000. This loan will be payable in 12 equal monthly installments of principal and interest. The loan will accrue interest at the rate of eight percent per annum and will mature on the 12-month anniversary of the closing of this transaction.

Rapid Link has also agreed to grant piggy-back registration rights to Telenational, whereby the Company will register the common stock issued in connection with the acquisition if Rapid Link files a registration statement after the closing date, subject to certain approvals and customary conditions and limitations.

The closing of the transactions contemplated by the Purchase Agreement and the Amendment took place on May 5, 2006.

### ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION.

The following discussion and analysis of financial condition and results of operations covers the three months ended April 30, 2006 and 2005 and should

## Edgar Filing: RAPID LINK INC - Form 10QSB

be read in conjunction with our financial statements and the notes thereto.

### FORWARD-LOOKING STATEMENTS

This quarterly report on Form 10-QSB contains "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These statements relate to expectations concerning matters that are not historical facts. Words such as "projects", "believe", "anticipates", "estimate", "plans", "expect", "intends", and similar words and expressions are intended to identify forward-looking statements. Although we believe that such forward-looking statements are reasonable, we cannot assure you that such expectations will prove to be correct. Factors that could cause actual results to differ materially from such expectations are disclosed in our annual report on Form 10-KSB for the year ended October 31, 2005 and throughout this report on Form 10-QSB. All of our forward-looking statements are expressly qualified in their entirety by such language and we do not undertake any obligation to update any forward-looking statements.

### General

On November 2, 1999, we acquired substantially all of the business and assets of Dial Thru International Corporation, a California corporation, and, on January 19, 2000, we changed our name from ARDIS Telecom & Technologies, Inc. to "Dial Thru International Corporation." In the second quarter of fiscal 2000, we shifted focus toward our global Voice over Internet Protocol, or VoIP, strategy. This strategy allows us to form local partnerships with foreign postal, telephone and telegraph companies (entities that are responsible for providing telecommunications services in foreign markets and which are usually government owned or controlled) and to provide IP enabled services based on the in-country regulatory environment affecting telecommunications and data providers.

On October 12, 2001, we completed the acquisition from Rapid Link, Incorporated ("RLI") of certain assets and executory contracts of Rapid Link, USA, Inc. and 100% of the common stock of Rapid Link Telecommunications, GmbH, a German company. RLI provided integrated data and voice communications services to both wholesale and retail customers around the world. RLI built a large retail customer base in Europe and Asia focusing mostly on the United States military sector, using RLI's network to make international calls anywhere in the world. Furthermore, RLI developed a VoIP network using Clarent and Cisco technology which we have used to take advantage of wholesale opportunities where rapid deployment and time to market are critical.

On August 1, 2003, our German subsidiary, Rapid Link Telecommunications GmbH, received approval for its insolvency filing and was turned over to a trustee who was responsible for liquidating the operation. We determined that we no longer controlled the operations of this subsidiary and that our parent entity has no legal obligation to pay the liabilities of Rapid Link Telecommunications GmbH.

On October 25, 2005, at our annual shareholders meeting, our shareholders approved a change in the Company's name to Rapid Link, Incorporated. The Company believes that the name "Rapid Link, Incorporated" better reflects the Company's business strategies and opportunities, and will receive better market recognition and acceptance than its previous name, especially as the Company continues to roll out Voice over Internet Protocol related services. In addition, the Company also believes that the name, which was the name of the Company we acquired in October 2001, is a recognized brand name with

## Edgar Filing: RAPID LINK INC - Form 10QSB

members of the United States Military around the world, a significant source of retail revenue for the Company since the acquisition. The name change became effective on November 1, 2005.

On October 31, 2005, we completed the acquisition of the customer base of Integrated Telecommunications, Inc., ("Integrated") an international long distance carrier providing Voice over Internet Protocol services to retail customers in the United States, and wholesale services to customers worldwide.

The telecommunications industry continues to evolve towards an increased emphasis on IP related products and services. We have focused our business towards these types of products and services for the last couple of years. Furthermore, we believe the use of the Internet to provide bundled IP related services to the end user customer, either as a stand alone solution or bundled with other IP products, will continue to impact the industry as large companies like Time Warner and AT&T look to capitalize on their existing cable infrastructures, and smaller companies look to provide innovative solutions to attract commercial and residential users to their product offerings.

We are focused on the growth of our VoIP business by adding new products and services that we can offer to end user customers. We are attempting to transition our current customers, and attract new customers through the sale of specialized VoIP Internet Access Devices, or IAD's, that allow customers to connect their phones to their existing high-speed Internet connections. These IADs allow the user to originate phone calls over the Internet, thereby bypassing the normal costs associated with originating phone calls over existing land lines. By avoiding these costs, we are able to offer lower priced services to these customers, which we believe will allow us to attract additional users. We also believe there will be considerable demand for this type of product in certain foreign markets where end users pay a significant premium to their local phone companies to make long distance or international phone calls. We are targeting business and residential customers, as well as niche markets, such as the United States military. While we expect the growth in our customers and suppliers, and the introduction of innovative product offerings to retail users, specifically IADs, to have a positive impact on our revenues and earnings, we cannot predict our ability to significantly grow this line of business. The revenue and costs associated with the IAD product offerings will depend on the number of customers and contracts we obtain. In many ways, our ability to maintain operations in the foreseeable future will be dictated by our ability to quickly deploy VoIP products into selected markets and to realize revenues from these products and related telecommunications sources. Any delay in our expansion of VoIP products and services will adversely affect our financial condition and cash flow and could ultimately cause us to greatly reduce or even cease operations.

Our common stock currently trades on the OTC Bulletin Board under the symbol "RPID."

We continue to seek opportunities to grow our business through strategic acquisitions that will complement our retail strategy as well as adding key personnel that have demonstrated a proven track record in sales, marketing and operations of retail telecommunications organizations, especially in the area of retail VoIP.

### Critical Accounting Policies

The consolidated financial statements include accounts of our Company and all of our majority-owned subsidiaries. The preparation of financial statements in conformity with accounting principles generally accepted in

## Edgar Filing: RAPID LINK INC - Form 10QSB

the United States requires us to make estimates and assumptions in certain circumstances that affect amounts reported in the accompanying consolidated financial statements and related footnotes. In preparing these financial statements, we have made our best estimates and judgments of certain amounts included in the financial statements, giving due consideration to materiality. We do not believe there is a great likelihood that materially different amounts would be reported related to estimates associated with the accounting policies described below. However, application of these accounting policies involves the exercise of judgment and use of assumptions as to future uncertainties and, as a result, actual results could differ from these estimates.

### Revenue Recognition

For a majority of our products, our revenues are generated at the time a customer uses our network to make a phone call. We sell our services to SMEs and end-users that utilize our network for international origination and dial thru services, and to other providers of long distance usage who utilize our network to deliver domestic and international termination of minutes to their own customers. At times we receive payment from our customers in advance of their usage, which we record as deferred revenue, recognizing revenue as calls are made.

For our newer VoIP product offerings, specifically our Rapid Link service, we are required to recognize revenue in accordance with Emerging Issues Task Force ("EITF") consensus No. 00-21, "Accounting for Revenue Arrangements with Multiple Deliverables" which requires that revenue arrangements with multiple deliverables be divided into separate units of accounting if the deliverables in the arrangement meet specific criteria. In addition, arrangement consideration must be allocated among the separate units of accounting based on their relative fair values, with certain limitations. The provisioning of the Rapid Link service with the accompanying desktop terminal adapter or other customer premise equipment constitutes a revenue arrangement with multiple deliverables. In accordance with the guidance of EITF No. 00-21, we allocate Rapid Link revenues, including activation fees, among the customer premise equipment and subscriber services. Revenues allocated to the customer premise equipment are recognized as product revenues at the end of 30 days after order placement, provided the customer does not cancel their Rapid Link service. All other revenues are recognized as license and service revenues when the related services are provided. We defer the cost of goods sold of products sold for which the end customer or distributor has a right of return. The cost of the products sold is recognized, contemporaneously with the recognition of revenue, when the subscriber has accepted the service.

The Securities and Exchange Commission's Staff Accounting Bulletin No. 104, "Revenue Recognition", provides guidance on the application of generally accepted accounting principles to selected revenue recognition issues. We have concluded that our revenue recognition policy is appropriate and in accordance with generally accepted accounting principles and Staff Accounting Bulletin No. 104.

### Allowance for Uncollectible Accounts Receivable

Accounts receivable are reduced by an allowance for amounts that may become uncollectible in the future. All of our receivables are due from commercial enterprises and residential users in both domestic and international markets. The estimated allowance for uncollectible amounts is based primarily on our evaluation of the financial condition of the customer, and our estimation of the customer's willingness to pay amounts due. We review our credit policies on a regular basis and analyze the risk of each prospective customer individually in order to minimize our risk.

## Edgar Filing: RAPID LINK INC - Form 10QSB

### Goodwill

Effective November 1, 2001, we adopted SFAS No. 141, "Business Combinations" ("SFAS 141") and SFAS No. 142, "Goodwill and Other Intangible Assets" ("SFAS 142"). SFAS 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, and also specifies the criteria for the recognition of intangible assets separately from goodwill. Under SFAS 142, goodwill is no longer amortized but is subject to an impairment test at least annually or more frequently if impairment indicators arise. In accordance with SFAS 142, an annual impairment test of goodwill was performed by an independent valuation firm in each of the fourth quarters of fiscal year 2005 and 2004. The valuation process appraised our assets and liabilities using a combination of present value and multiple of earnings valuation techniques. The results of both impairment tests indicated goodwill was not impaired.

We record goodwill when the consideration paid for an acquisition exceeds the fair value of net tangible and identifiable intangible assets acquired. We measure and test goodwill for impairment on an annual basis or more frequently if we believe indicators of impairment exists. Performance of the impairment test involves a two-step process. The first step compares the fair value of our single reporting unit to its carrying amount. The fair value of the reporting unit is determined by calculating the market capitalization of the reporting unit as derived from quoted market prices, and further substantiated through the use of other generally accepted valuation methods. A potential impairment exists if the fair value of the reporting unit is lower than its carrying amount. Historically, the impairment test has shown that the carrying value is less than fair value. The second step of the process is only performed if a potential impairment exists, as indicated by step one, and involves determining the difference between the fair values of the reporting unit's net assets, other than goodwill, as compared to the fair value of the reporting unit. If the difference is less than the net book value of goodwill, impairment exists and is recorded. We determine our reporting units, for purposes of testing for impairment, by determining (i) how we manage our operations, (ii) if a component of an operating unit constitutes a business for which discrete financial information is available and our management regularly review such financial information, and (iii) how the acquired entity is integrated with our operations. Based on these criteria, we determined that we have a single reporting unit.

In order to determine the fair value of our reporting unit under SFAS 142, we considered the following two approaches:

- \* Market Approach - Under the market approach, recent sales of comparable companies or securities are analyzed to determine the value for a particular asset under study. Adjustments are made to the sales data to account for differences between the subject asset and the comparables. The market approach is most applicable to assets that are homogenous in nature and are actively traded. Relative to other approaches to value, the key strength of the market approach is that it provides objective indications of value while requiring relatively few assumptions be made.
- \* Income Approach - This approach measures the present worth of anticipated future net cash flows generated by the business. Net cash flows are forecast for an appropriate period and then discounted to present value using an appropriate discount rate. Net cash flow forecasts require analysis of the significant variables influencing revenues, expenses, working capital,



## Edgar Filing: RAPID LINK INC - Form 10QSB

and capital investment. An income approach methodology is generally useful because it accounts for the specific contribution of fundamental factors impacting those variables that affect the value of the business.

According to SFAS 142, quoted market prices in active markets are the best evidence of fair value and shall be used as the basis for the measurement of fair value, if available. As of October 31, 2005, our market capitalization was \$3,222,690, determined by taking the shares outstanding as of that date multiplied by our stock price of \$0.11. We added interest bearing debt and operating liabilities (excluding net current liabilities of discontinued operations), adjusted downward to a fair value estimate of 25%, resulting in a fair value of assets of approximately \$5.3 million. This amount exceeds the carrying value of our assets (the value of our assets as reported in our financial statements), including goodwill, of \$3,218,596. While our market capitalization renders a minority interest valuation, because shares of our Company represent minority interests, the fair value of assets exceeds its carrying value even without the application of a control premium as recommended by SFAS 142. However, we believe that the application of the market approach necessitates additional analysis for three reasons (i) we have generated no analyst coverage to provide information about our stock to the public, suggesting that the market price may not reflect available information, (ii) our stock price demonstrated volatility as of the valuation date, and (iii) our stock is thinly traded with no organization making an active market in the stock. These factors suggest that our stock price, when taken in isolation, may not be sufficient evidence of fair value. In estimating the fair value of a reporting unit, a valuation technique based on multiples of earnings or revenues or a similar performance measure may be used if that technique is consistent with the objective of measuring fair value. As further support for our market approach, we calculated the Business Enterprise Value ("BEV") for five other telecommunications companies, which provide services similar to those that we provide. The BEV is determined by taking the market capitalization of a public enterprise, adding their debt and subtracting any cash equivalents. The resulting value is divided by annual revenue in order to determine a reasonable multiple that can be applied to us. We averaged the multiple of these five companies, trading on average at 2.6 times their annual revenue obtained from their most recent published financials, and applied the result to our 2005 fiscal year revenues. The resulting BEV for our Company was well in excess of the fair value of our assets calculated above. As a result, we determined that the fair value of our Company exceeds its carrying amount, and therefore that goodwill is not impaired.

### Financing, Warrants and Amortization of Warrants and Fair Value Determination

We have traditionally financed our operations through the issuance of debt instruments that are convertible into our common stock, at conversion rates at or below the fair market value of our common stock at the time of conversion, and typically include the issuance of warrants. We have recorded debt discounts in connection with these financing transactions in accordance with Emerging Issues Task Force Nos. 98-5 and 00-27. Accordingly, we recognize the beneficial conversion feature imbedded in the financings and the fair value of the related warrants on the balance sheet as debt discount. The debt discount is amortized over the life of the respective debt instrument.

### Carrier Disputes

We review our vendor bills on a monthly basis and periodically dispute amounts invoiced by our carriers. We review our outstanding disputes on a quarterly basis, as part of the overall review of our accrued carrier costs, and adjust our liability based on management's estimate of amounts owed.

## Edgar Filing: RAPID LINK INC - Form 10QSB

### RESULTS OF OPERATIONS

The following table presents our operating results for the three and six month periods ended April 30, 2006 and 2005 as well as a comparison of the percentage change of our operating results from the three and six month periods ended April 30, 2006 to the corresponding periods ended April 30, 2005:

	3 months Ended April 30,		% of Revenue 3 months Ended April 30,		6 months Ended April 30,	
	2006	2005	2006	2005	2006	2005
REVENUES	\$2,121,018	\$2,864,960	100%	100%	\$4,107,130	\$5,649,960
COSTS AND EXPENSES						
Costs of revenues	1,612,960	2,385,165	76%	83%	3,141,075	4,382,960
Sales and marketing	99,827	42,919	5%	1%	242,209	97,000
General and administrative	732,995	849,937	35%	30%	1,390,419	1,600,000
Depreciation and amortization	99,967	150,415	5%	5%	204,179	296,000
Gain on disposal of equipment	34,229	-	0%	0%	34,229	(8,000)
Total costs and expenses	2,579,978	3,428,436	122%	120%	5,012,111	6,367,960
Operating loss	(458,960)	(563,476)	-22%	-20%	(904,981)	(718,000)
OTHER INCOME (EXPENSE)						
Interest expense and financing costs	(355,370)	(54,092)	-17%	-2%	(603,751)	(108,000)
Related party interest expense and financing costs	(33,357)	(36,772)	-2%	-1%	(66,414)	(73,000)
Foreign currency exchange gains	1,358	(2,788)	0%	0%	23,641	7,000
Total other expense, net	(387,369)	(93,652)	-18%	-3%	(646,524)	(174,000)
NET INCOME (LOSS)	\$ (846,329)	\$ (657,128)	-40%	-23%	\$ (1,551,505)	\$ (893,000)

### RESULTS OF OPERATIONS - COMPARISON OF THE THREE MONTH AND SIX MONTH PERIODS ENDED APRIL 30, 2006 and 2005

#### REVENUES

For the three-month period ended April 30, 2006, 58% and 42%, of our revenues were derived from our wholesale and retail customers, respectively, compared to 77% and 23%, respectively, for the three-month period ended April 30, 2005. Our wholesale revenues have decreased by 44% from the three-month period ended April 30, 2005 compared to the three-month period ended April 30, 2006, while our retail revenues have increased by 34% during the three month period ended April 30, 2006 over the comparable period in 2005.

For the six-month period ended April 30, 2006, 56% and 44%, of our revenues were derived from our wholesale and retail customers, respectively, compared

## Edgar Filing: RAPID LINK INC - Form 10QSB

to 74% and 26%, respectively, for the six-month period ended April 30, 2005. Our wholesale revenues have decreased by 45% from the six-month period ended April 30, 2005 compared to the six-month period ended April 30, 2006, while our retail revenues have increased by 21% during the six month period ended April 30, 2006 over the comparable period in 2005.

The decrease in wholesale revenues for the three month period ended April 30, 2006 compared to the same period in fiscal 2005 is attributable to the Company's change in focus from its wholesale opportunities to its new VoIP retail opportunities.

The increase in retail revenues for the three month period ended April 30, 2006 compared to the same period in fiscal 2005 is attributable to the Company's focus on retail revenue and the acquisition of the customer base of Integrated. We continue to experience increased competition in our largest foreign markets, including competition from the incumbent phone company in each market. Furthermore, a significant portion of our retail business comes from members of the United States military stationed in foreign markets. The March 2003 redeployment of troops into Iraq, where we have not historically provided long distance service, resulted in a decline in our retail sales to these military customers who were previously stationed in foreign markets that we serviced. We are currently able to offer VoIP services into Iraq, with the hope of recapturing some of our prior customers who have been transferred to Iraq and other Middle Eastern Countries. We are exploring opportunities to grow our retail business, utilizing our in-house sales group and our outside agents, through the introduction of new products and services, focusing our efforts principally on the sale of VoIP services which allow users to make phone calls over an existing broadband internet connection. Furthermore, we will continue to seek out acquisitions that will allow us to quickly grow our business in the different niche markets we are targeting. If we are unable to stabilize our retail revenues from the U.S. military and grow our retail revenues from VoIP-based products, our retail revenues may remain flat or decline.

### COSTS OF REVENUES

Our costs of revenues as a percentage of revenues have decreased 7% from 83% for the three-month period ended April 30, 2005 to 76% for the three-month period ended April 30, 2006. This decrease was primarily due to a change in the mix of our revenue with a greater percentage of our revenue coming from our retail products, which realize a higher margin than our wholesale services. As a majority of our costs of revenues are variable, based on per minute transportation costs, costs of revenues as a percentage of revenues will fluctuate, from period to period, depending on the traffic mix between our wholesale and retail products and total revenue for each period.

Our costs of revenues as a percentage of revenues have decreased 2% from 78% for the six-month period ended April 30, 2005 to 76% for the six-month period ended April 30, 2006. Included within our costs of revenues for the six-month period ended April 30, 2005 is a reduction of costs in the amount of \$283,138 relating to the favorable resolution of a dispute with one of our vendors. These costs were originally recorded to costs of revenues in prior periods. Had this dispute resolution not occurred during the six-month period ended April 30, 2005, our costs of revenues as a percentage of revenues would have decreased by 7% for the six-month period ended April 30, 2006 compared to the six-month period ended April 30, 2005.

### SALES AND MARKETING EXPENSES

A significant component of our revenue is generated by outside agents or through periodic newspaper advertising, which is managed by a small in-house sales and marketing organization.

## Edgar Filing: RAPID LINK INC - Form 10QSB

Our sales and marketing costs have increased from 1% to 5% and 2% to 6% of revenues, respectively, for the three and six month periods ended April 30, 2006 compared to the prior year period. The increase in our sales and marketing costs is primarily due to additional personnel and commission's incurred as a result of the Integrated acquisition. During the three month period ended April 30, 2006, we have focused our attention on increasing revenues through the efforts of our agents and the initiation of advertising on military websites. We will continue to focus our sales and marketing efforts on periodic newspaper and internet advertising, the establishment of distribution networks to facilitate the introduction and growth of new products and services, and agent related expenses to generate additional revenues.

### GENERAL AND ADMINISTRATIVE EXPENSES

Our general and administrative expenses have increased to 35% and 34% of revenues for the three and six months ended April 30, 2006 from 30% and 28% for the three and six months ended April 30, 2005. Although general and administrative expenses as a percentage of revenues have increased for the three and six months ended April 30, 2006 compared to the prior fiscal year, in absolute dollars, general and administrative expenses have decreased by approximately \$117,000 and \$210,000, respectively. This reduction has been accomplished primarily through the elimination of personnel and personnel related costs, consulting and professional fees and bad debt expense. However, due to the overall decline in revenue and the primarily fixed nature of our general and administrative expenses, as a percentage of revenue, these expenses have increased for the three months ended April 30, 2006 compared to the prior period. We review our general and administrative expenses regularly and continue to manage the costs accordingly to support our current and anticipated future business, however it will be difficult to achieve significant reductions in future periods due to the fixed nature of our general and administrative expenses without accretive acquisitions in the future.

### DEPRECIATION AND AMORTIZATION

Depreciation and amortization has decreased primarily as the result of significant components of our property and equipment reaching the end of their useful lives each quarter. Our major property and equipment additions were the result of the RLI acquisition in fiscal 2001. In addition, depreciation and amortization has decreased as we have disposed of certain telecommunications switching equipment that was not in use.

### INTEREST EXPENSE AND FINANCING COSTS

Interest expense and financing costs including related party interest expense and financing costs, for the three month period ended April 30, 2006 and 2005 were due primarily to interest expense of approximately \$86,000 and \$90,000, respectively, on our convertible debentures and notes payable to related parties. In addition, for the three month period ended April 30, 2006, interest expense includes approximately \$301,000 of amortization of deferred financing fees and debt discount relating to the extension of the maturity dates on our debts to GCA, Global and related parties. The increase in interest expense and financing costs from the three months ended April 30, 2005 to the three month period ended April 30, 2006 primarily relates to the extension of the maturity dates of our convertible debt instruments with both our third party and related party lenders during the third quarter of fiscal 2005.

Interest expense and financing costs including related party interest expense and financing costs, for the six month period ended April 30, 2006

## Edgar Filing: RAPID LINK INC - Form 10QSB

and 2005 were due primarily to interest expense of approximately \$161,000 and \$182,000, respectively, on our convertible debentures and notes payable to related parties. In addition, for the six month period ended April 30, 2006, interest expense includes approximately \$509,000 of amortization of deferred financing fees and debt discount relating to the extension of the maturity dates on our debts to GCA, Global and related parties. The increase in interest expense and financing costs from the six months ended April 30, 2005 to the six month period ended April 30, 2006 primarily relates to the extension of the maturity dates of our convertible debt instruments with both our third party and related party lenders during the third quarter of fiscal 2005.

### LIQUIDITY AND CAPITAL RESOURCES

Our operating loss for the three and six months ended April 30, 2006 over the prior comparable periods has increased and to date we have been unable to achieve positive cash flow on a quarterly basis primarily due to the fact that our present lines of business do not generate a volume of business sufficient to cover our overhead costs. Our audit report for the fiscal year ended October 31, 2005 includes an explanatory paragraph indicating substantial doubt about our ability to continue as a going concern.

We have violated certain requirements of our convertible debt agreements relating to failure to register the underlying securities, and timely payment of principal and interest, including payment in full on the maturity date of the notes, either through the issuance of common stock, or payment in cash. Our lenders have not declared us in default and have allowed us to continue to operate. On June 1, 2005, we and our third-party lenders agreed to amendments to our notes payable and convertible debenture agreements to extend the maturity dates to various times ranging from November 26, 2006 through February 29, 2008. Approximately \$1.9 million of principal and interest is due to two of our executives and a director.

Furthermore, we frequently are not able to make timely payment to our trade creditors. As of April 30, 2006, approximately \$4.3 million, representing approximately 74% of our trade accounts payable and accrued liabilities, were past due. A majority of the amounts past due are to foreign vendors that have supplied us with low margin wholesale opportunities and we are no longer sending significant, or any, telecommunications traffic to them. We will continue to work with them to arrange for a reduction in the amount owed to them through either formal or informal payment plans. We continue to seek sources of working capital sufficient to fund delinquent balances and meet ongoing obligations, though our success on this process has been limited.

Our future operating success is dependent on our ability to generate positive cash flow from our existing products and services and/or accretive acquisitions. Our major growth areas are through the introduction of new retail VoIP products, both domestically and internationally. We anticipate a \$400,000-600,000 cash shortfall from operations during the next 12 months; however we are currently pursuing retail opportunities and acquisitions that we believe will reduce this shortfall immediately. There can be no assurance that we will be successful in implementing these opportunities. We do not have any capital equipment commitments during the next 12 months. We are actively pursuing debt or equity financing opportunities to continue our business. Any failure of our business plan, including the risk and timing involved in rolling out retail products to end users, to generate positive cash flow could result in a significant cash flow crisis and could force us to seek alternative sources of financing as discussed, or to greatly reduce or discontinue operations. Although various possibilities for obtaining financing or effecting a business combination have been discussed from time to time, and we are having ongoing discussions with several potential

## Edgar Filing: RAPID LINK INC - Form 10QSB

financing sources, there are no definitive agreements with any party to raise money and we cannot assure you that we will be successful in our search for investors or lenders. However, the acquisition of Telenational (see Note 9 - Subsequent events) was consummated May 5, 2006, thus changing the financial position of the Company substantially. Any additional financing we may obtain may involve material and substantial dilution to existing stockholders. In such event, the percentage ownership of our current stockholders may be materially reduced, and any new equity securities sold by us may have rights, preferences or privileges senior to our current common stockholders. If we are unable to obtain additional financing, our operations in the short term may be materially affected and we may not be able to remain in business. These circumstances raise substantial doubt as to the ability of our Company to continue as a going concern.

On March 8, 2006, the Company completed a private placement of two one year 10% convertible debentures ("Debentures"), for gross proceeds of \$1,000,000. In connection with the Debentures, the Company agreed to issue the investors a total of 2,000,000 immediately exercisable five year warrants to purchase the Company's common stock at an exercise price of \$0.14 for 1,000,000 warrants, and \$0.25 for an additional 1,000,000 warrants. In addition, the investors will receive an additional 50,000 warrants to vest and become exercisable on the last day of each month prior to the Company's satisfaction in full of the Debentures or the complete conversion of the Debentures, at an exercise price of \$0.25. A portion of the proceeds have been used to repay the Advances from Shareholder (see Note 7 - Advances from Shareholder).

At April 30, 2006, we had cash and cash equivalents of \$168,000, a decrease of \$4,000 from the balance at October 31, 2005. We had significant working capital deficits at both April 30, 2006 and October 31, 2005.

Net cash used in operating activities was \$886,000 for the six months ended April 30, 2006. The net cash used in operating activities for the six months ended April 30, 2006 was primarily due to a net loss of \$1.6 million adjusted for: non-cash interest expense of \$510,000, and depreciation and amortization of \$204,000. Net cash provided by operating activities was \$24,000 for the six months ended April 30, 2006. For the six month period ended April 30, 2005, the net cash provided by operating activities was due to a net loss from continuing operations of \$893,000 adjusted for depreciation and amortization of \$269,000, warrants issued for services of \$160,000, and net changes in operating assets and liabilities of (\$490,000).

Net cash used in investing activities for the six-month periods ended April 30, 2006 and 2005 was \$74,000 and \$13,000, respectively, and primarily relates to the purchase of property and equipment.

Net cash provided by financing activities for the six months ended April 30, 2006 was \$956,000. This amount represents proceeds received from a note payable due to Trident Growth Fund L.P. and Charger Investments LLC, less financing fees paid. During the three months ended January 31, 2006, the Company's chief executive officer, and significant shareholder, John Jenkins, advanced funds to the Company in the aggregate amount of \$500,000. During the three-month period ended April 30, 2006 the Company has re-paid this amount in full with proceeds received from the Debentures.

We have an accumulated deficit of approximately \$50.7 million as of April 30, 2006 as well as a significant working capital deficit. Funding of our working capital deficit, current and future operating losses, and expansion will require continuing capital investment which may not be available to us. Since the beginning of April 2001, we have raised \$6.7 million in debt financing.

## Edgar Filing: RAPID LINK INC - Form 10QSB

Although to date we have been able to arrange debt facilities and equity financing, there can be no assurance that sufficient debt or equity financing will continue to be available in the future or that it will be available on terms acceptable to us. As of April 30, 2006 we have approximately \$2,207,000 principal balance of convertible debentures which will mature within the next year as well as a significant amount of trade payables and accrued liabilities which are past due. We will continue to explore external financing opportunities in order to fund these past due amounts. Our management is committed to the success of our Company as is evidenced by the level of financing it has made available to our Company. Failure to obtain sufficient capital will materially affect our Company's operations and financial condition. As a result of the aforementioned factors and related uncertainties, there is significant doubt about our Company's ability to continue as a going concern.

Our current capital expenditure requirements are not significant, primarily due to the equipment acquired from Rapid Link. We do not anticipate significant spending for the remainder of fiscal year 2006.

In October 2001, we executed 10% convertible notes (the "Notes") with three of our executives, which provided financing of \$1,945,958. With an original maturity date of October 24, 2003, these Notes were amended subsequent to fiscal year 2002 to extend the maturity date to February 24, 2004. These Notes are secured by selected Company assets and are convertible into our common stock at the option of the holder at any time. The conversion price is equal to the closing bid price of our common stock on the last trading day immediately preceding the conversion. We also issued to the holders of the Notes warrants to acquire an aggregate of 1,945,958 shares of common stock at an exercise price of \$0.78 per share, which expire on October 24, 2006. For the year ended October 31, 2002, an additional \$402,433 was added to the Notes and an additional 402,433 warrants to acquire our common stock were issued in connection with the financing. During fiscal year 2004, the holders of the Notes elected to convert \$877,500 of the Notes into 6,750,000 shares of our common stock. On July 21, 2005, the Company and the three executives agreed to extend the maturity date of the Notes to February 29, 2008. In connection with the extension, the Company issued to the three executives warrants to acquire 640,000 shares of common stock at an exercise price of \$0.16. The warrants expire in July 2010. The gross outstanding balance of these Notes at April 30, 2006 totals \$1,003,390.

In January 2002, we executed a 6% convertible debenture (the "Debenture") with GCA Strategic Investment Fund Limited ("GCA"), which provided financing of \$550,000 and had an original maturity date of January 28, 2003. We also issued to the holder of the Debenture warrants to acquire an aggregate of 50,000 shares of common stock at an exercise price of \$0.41 per share, which expire on January 28, 2007. The Debenture was amended in January 2003 to extend the maturity date to November 8, 2004. In connection with this January 2003 amendment we adjusted the exercise price of the previously issued warrants to \$0.21 per share and also issued to the holder of the Debenture warrants to acquire an aggregate of 100,000 shares of common stock at an exercise price of \$0.21 per share, which expire on February 8, 2008. The Debenture was amended again in June 2005 to extend the maturity date to November 26, 2005. On March 8, 2006, the Debenture was amended again to extend the maturity date to November 26, 2006. In connection with this June 2005 amendment of the Debenture, we also issued to the holder of the Debenture 100,000 shares of our common stock, warrants to purchase 150,000 shares of our common stock at an exercise price of \$0.38 per share and warrants to purchase 110,000 shares of our common stock at an exercise price of \$0.11 per share, all of which warrants expire on June 1, 2010. The conversion price of the Debenture is equal to the lesser of (i) 100% of the volume weighted average of sales price as reported by the Bloomberg L.P. of

## Edgar Filing: RAPID LINK INC - Form 10QSB

the common stock on the last trading day immediately preceding the closing date and (ii) 85% of the average of the three lowest volume weighted average sales prices as reported by Bloomberg L.P. during the 20 trading days immediately preceding but not including the date of the related notice of conversion (the "Formula Conversion Price"). In an event of default the amount declared due and payable on the Debenture shall be automatically converted into shares of our common stock at the Formula Conversion Price. During fiscal year 2003, GCA converted \$50,000 of the Debenture and \$3,463 of accrued interest into approximately 374,000 shares of common stock. During fiscal year 2004, GCA converted \$10,000 of the Debenture and \$730 of accrued interest into approximately 82,000 shares of our common stock. During fiscal year 2005, GCA converted \$35,000 of the Debenture and \$7,770 of accrued interest into approximately 352,000 shares of our common stock. During fiscal year 2006, GCA converted \$25,000 of the Debenture and \$6,150 of accrued interest into approximately 407,000 shares of common stock. The gross outstanding balance on the Debenture was \$430,000 at April 30, 2006.

In November 2002, we executed a 12% note payable (the "GC-Note") with Global Capital Funding Group, L.P., ("Global") which provided financing of \$1,250,000. The GC-Note matured on November 8, 2004. We also issued to the holder of the GC-Note warrants to acquire an aggregate of 500,000 shares of common stock at an exercise price of \$0.14 per share, which expire on November 8, 2007. In June 2005, the GC-Note was replaced by a convertible note ("GC-Conote"). The GC-Conote matures on February 29, 2008, and the annual interest rate due on this convertible note is 10.08%. The conversion price is equal to 80% of the average of the three (3) lowest volume weighted average sales prices as reported by Bloomberg L.P. during the twenty (20) trading days immediately preceding the date of the related notice of conversion. In addition, we issued to the holder of the GC-Conote 100,000 shares of our common stock, warrants to purchase 500,000 shares of our common stock at an exercise price of \$0.38 per share and warrants to purchase 125,000 shares of our common stock at an exercise price of \$0.11 per share, all of which warrants expire on June 1, 2010. In addition, interest of approximately \$350,000 due on the GC-Note at the time of replacement by the GC-Conote was converted into a \$400,000 non-interest bearing note payable ("GC-Note2"), which matures on March 30, 2007. The approximate \$50,000 difference between the accrued interest at the time of replacement and the value of this new note was recorded as deferred financing fees, and is being amortized over the life of the GC-Note2. During fiscal year 2006 GCA elected to convert \$50,000 of the GC-Note2 into approximately 694,000 shares of common stock. The gross outstanding balance of the GC-Note2 was \$225,000 at April 30, 2006.

In July 2003, we executed a 10% note payable (the "GCA-Note") with GCA Strategic Investment Fund Limited, which provided financing of \$550,000. The GCA-Note's maturity date was December 23, 2003. We also issued to the holder of the GCA-Note warrants to acquire an aggregate of 100,000 shares of common stock at an exercise price of \$0.14 per share, which expire on July 24, 2008. Per the terms of the GCA-Note agreement, in the event the GCA-Note is not repaid in full within ten days of the maturity date, the terms of the GCA-Note shall become the same as those of the Debenture. Effective January 2, 2004, the GCA-Note was replaced by a convertible debenture ("GCA-Debenture") with the same terms as those of the Debenture, which had a maturity date of November 8, 2004. The principal balance of the GCA-Debenture was \$574,597, which included \$24,597 of interest due on the GCA-Note at the time it was replaced by the GCA-Debenture. The GCA-Debenture was amended in June 2005, to extend the maturity date to November 26, 2006. In connection with this amendment, we also issued to the holder of the GCA-Debenture 40,000 shares of our common stock, and warrants to purchase 150,000 shares of our common stock at an exercise price of \$0.38 per share, which warrants expire on June 1, 2010. The gross outstanding balance on the GCA-Debenture was approximately \$550,000 at April 30, 2006.



## Edgar Filing: RAPID LINK INC - Form 10QSB

On March 8, 2006, the Company completed a private placement of two one year 10% convertible debentures ("Debentures"), for gross proceeds of \$1,000,000. In connection with the Debentures, the Company agreed to issue the investors a total of 2,000,000 immediately exercisable five year warrants to purchase the Company's common stock at an exercise price of \$0.14 for 1,000,000 warrants, and \$0.25 for an additional 1,000,000 warrants. The Company paid \$44,150 in financing fees in connection with the debentures which were recorded as a discount on the debentures. Additionally in connection with these Debentures the Company recorded a debt discount of \$1,000,000 related to the fair value of warrants issued and the related beneficial conversion feature that it will amortize over the life of the loan.

During the three months ended January 31, 2006, the Company's chief executive officer, and significant shareholder, John Jenkins, advanced funds to the Company in the aggregate amount of \$500,000. During the three-month period ended April 30, 2006 the Company has re-paid this amount in full with proceeds received from financing.

### Risk Factors

An investment in us involves a high degree of risk and should be undertaken only by persons whose financial resources are sufficient to enable them to assume such risk and to bear the total loss of their investment. This section sets forth a brief summary of some of the principal risk factors. If the Company is unable to address and deal with one or more of the risks described below or any other risks which it may face, then its business, operating results and financial condition could be materially adversely affected, and you could lose all or part of your investment. For these reasons, prospective investors should carefully consider the risks described below as well as any other possible risks that could be important.

Our cash flow may not be sufficient to satisfy our operations

For the three and six month period ended April 30, 2006, we recorded a net loss of approximately \$846,000 and \$1,551,000, and for the year ended October 31, 2005, we recorded a net loss of approximately \$2,565,000. As a result of these losses, and prior losses, we currently have a significant working capital deficit. In addition, we have a significant amount of trade accounts payables and accrued liabilities, of which approximately 74% is past due. To be able to service our debt obligations over the remainder of the 2006 fiscal year we must generate significant cash flow and obtain additional financing. If we are unable to do so or otherwise unable to obtain funds necessary to make required payments on our trade debt and other indebtedness, it is likely that we will not be able to continue our operations.

Our independent auditors have included a going concern paragraph in their audit opinion on our consolidated financial statements for the fiscal year ended October 31, 2005, which states that "The Company has suffered recurring losses from continuing operations during each of the last two fiscal years. Additionally, at October 31, 2005, the Company's current liabilities (which includes significant amounts of past due payables) exceeded its current assets by \$7.7 million and the Company has a shareholders' deficit totaling \$6.8 million. These conditions raise substantial doubt about the Company's ability to continue as a going concern."

Our operating history makes it difficult to accurately assess our general prospects in the VoIP portion of the telecommunications industry and the effectiveness of our business strategy. In addition, we have limited meaningful historical financial data upon which to forecast our future sales

## Edgar Filing: RAPID LINK INC - Form 10QSB

and operating expenses. Our future performance will also be subject to prevailing economic conditions and to financial, business and other factors. Accordingly, we cannot assure you that we will successfully implement our business strategy or that our actual future cash flows from operations will be sufficient to satisfy our debt obligations and working capital needs.

To implement our business strategy, we will also need to seek additional financing. There is no assurance that adequate levels of additional financing will be available at all or on acceptable terms. In addition, any additional financing will likely result in significant dilution to our existing stockholders. If we are unable to obtain additional financing on terms that are acceptable to us, we could be forced to dispose of assets to make up for any shortfall in the payments due on our debt under circumstances that might not be favorable to realizing the highest price for those assets. A portion of our assets consist of intangible assets, the value of which will depend upon a variety of factors, including the success of our business. As a result, if we do need to sell any of our assets, we cannot assure you that our assets could be sold quickly enough, or for amounts sufficient, to meet our obligations.

We face competition from numerous, mostly well-capitalized sources

The market for our products and services is highly competitive. We face competition from multiple sources, virtually all of which have greater financial resources and a substantial presence in our markets and offer products or services similar to our services. Therefore, we may not be able to successfully compete in our markets, which could result in a failure to implement our business strategy, adversely affecting our ability to attract and retain new customers. In addition, competition within the industries in which we operate is characterized by, among other factors, price and the ability to offer enhanced services. Significant price competition would reduce the margins realized by us in our telecommunications operations. Many of our competitors have greater financial resources to devote to research, development and marketing, and may be able to respond more quickly to new or merging technologies and changes in customer requirements. If we are unable to provide value-added Internet products and services then we will be unable to compete in certain segments of the market, which could have an adverse impact on our business.

The regulatory environment in our industry is very uncertain

The legal and regulatory environment pertaining to the Internet is uncertain and changing rapidly as the use of the Internet increases. For example, in the United States, the FCC is considering whether to impose surcharges or additional regulations upon certain providers of Internet telephony.

In addition, the regulatory treatment of Internet telephony outside of the United States varies from country to country. There can be no assurance that there will not be legally imposed interruptions in Internet telephony in these and other foreign countries. Interruptions or restrictions on the provision of Internet telephony in foreign countries may adversely affect our ability to continue to offer services in those countries, resulting in a loss of customers and revenues.

New regulations could increase the cost of doing business over the Internet or restrict or prohibit the delivery of our products or services using the Internet. In addition to new regulations being adopted, existing laws may be applied to the Internet. Newly existing laws may cover issues that include sales and other taxes, access charges, user privacy, pricing controls, characteristics and quality of products and services, consumer protection, contributions to the Universal Service Fund, an FCC-administered fund for the support of local telephone service in rural and high-cost areas, cross-

## Edgar Filing: RAPID LINK INC - Form 10QSB

border commerce, copyright, trademark and patent infringement, and other claims based on the nature and content of Internet materials.

Changes in the technology relating to Internet telephony could threaten our operations

The industries in which we compete are characterized, in part, by rapid growth, evolving industry standards, significant technological changes and frequent product enhancements. These characteristics could render existing systems and strategies obsolete and require us to continue to develop and implement new products and services, anticipate changing consumer demands and respond to emerging industry standards and technological changes. No assurance can be given that we will be able to keep pace with the rapidly changing consumer demands, technological trends and evolving industry standards.

We need to develop and maintain strategic relationships around the world to be successful

Our international business, in part, is dependent upon relationships with distributors, governments or providers of telecommunications services in foreign markets. The failure to develop or maintain these relationships could have an adverse impact on our business.

We rely on three key senior executives

Our success is dependent on our senior management team of John Jenkins, David Hess and Chris Canfield and our future success will depend, in large part, upon our ability to retain these three individuals.

The expansion of our VoIP product offerings is essential to our survival

We intend to expand our VoIP network and the range of enhanced telecommunications services that we provide. Our expansion prospects must be considered in light of the risks, expenses and difficulties frequently encountered by companies in new and rapidly evolving markets.

Our OTC Bulletin Board listing negatively affects the liquidity of our common stock

Our common stock currently trades on the OTC Bulletin Board. Therefore, no assurances can be given that a liquid trading market will exist at the time any stockholder desires to dispose of any shares of our common stock. In addition, our common stock is subject to the so-called "penny stock" rules that impose additional sales practice requirements on broker-dealers who sell such securities to persons other than established customers and accredited investors (generally defined as an investor with a net worth in excess of \$1 million or annual income exceeding \$200,000, or \$300,000 together with a spouse). For transactions covered by the penny stock rules, a broker-dealer must make a suitability determination for the purchaser and must have received the purchaser's written consent to the transaction prior to sale. Consequently, both the ability of a broker-dealer to sell our common stock and the ability of holders of our common stock to sell their securities in the secondary market may be adversely affected. The Securities and Exchange Commission has adopted regulations that define a "penny stock" to be an equity security that has a market price of less than \$5.00 per share, subject to certain exceptions. For any transaction involving a penny stock, unless exempt, the rules require the delivery, prior to the transaction, of a disclosure schedule relating to the penny stock market. The broker-dealer must disclose the commissions payable to both the broker-dealer and the registered representative, current quotations for the securities and, if the broker-dealer is to sell the securities as a

## Edgar Filing: RAPID LINK INC - Form 10QSB

market maker, the broker-dealer must disclose this fact and the broker-dealer's presumed control over the market. Finally, monthly statements must be sent disclosing recent price information for the penny stock held in the account and information on the limited market in penny stocks.

### ITEM 3. CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures. Our management carried out an evaluation, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that as of the end of the period covered by this report, our disclosure controls and procedures were effective. Disclosure controls and procedures mean our controls and other procedures that are designed to ensure that information required to be disclosed by us in our reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in our reports that we file or submit under the Securities Exchange Act of 1934 is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

(b) Changes in Internal Controls. There have been no changes in our internal control over financial reporting that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

### PART II. OTHER INFORMATION

#### Item 6. Exhibits and Reports on Form 8-K.

##### (a) Exhibits

- 2.1 Agreement and Plan of Merger dated as of January 30, 1998, among Canmax Inc., CNMX MergerSub, Inc. and US Communications Services, Inc. (filed as Exhibit 2.1 to Form 8-K dated January 30, 1998 (the "USC 8-K"), and incorporated herein by reference)
- 2.2 Rescission Agreement dated June 15, 1998 among Canmax Inc., USC and former principals of USC (filed as Exhibit 10.1 to Form 8-K dated January 15, 1998 (the "USC Rescission 8-K"), and incorporated herein by reference)
- 2.3 Asset Purchase Agreement by and among Affiliated Computed Services, Inc., Canmax and Canmax Retail Systems, Inc. dated September 3, 1998 (filed as Exhibit 10.1 to the Company's Form 8-K dated December 7, 1998 and incorporated herein by reference)
- 2.4 Asset Purchase Agreement dated November 2, 1999 among ARDIS Telecom & Technologies, Inc., Dial Thru International Corporation, a Delaware corporation, Dial Thru International Corporation, a California corporation, and John Jenkins (filed as Exhibit 2.1 to the Company's Current Report on Form 8-K dated November 2, 1999 and incorporated herein by reference)

## Edgar Filing: RAPID LINK INC - Form 10QSB

- 2.5 Stock and Asset Purchase Agreement, dated as of September 18, 2001, by and among Rapid Link USA, Inc., Rapid Link Inc., and Dial Thru International Corporation. (filed as Exhibit 2.1 to the Company's Form 8-K dated October 29, 2001 and incorporated herein by reference)
- 2.6 First Amendment to Stock and Asset Purchase Agreement, dated as of September 21, 2001, by and among Rapid Link USA, Inc., Rapid Link Inc., and Dial Thru International Corporation. (filed as Exhibit 2.2 to the Company's Form 8-K dated October 29, 2001 and incorporated herein by reference)
- 2.7 Second Amendment to Stock and Asset Purchase Agreement, dated as of October 12, 2001, by and among Rapid Link USA, Inc., Rapid Link Inc., and Dial Thru International Corporation. (filed as Exhibit 2.3 to the Company's Form 8-K dated October 29, 2001 and incorporated herein by reference)
- 2.8 Third Amendment to Stock and Asset Purchase Agreement, dated as of October 30, 2001, by and among Rapid Link USA, Inc., Rapid Link Inc., and Dial Thru International Corporation. (filed as Exhibit 2.4 to the Company's Form 8-K dated December 28, 2001 and incorporated herein by reference)
- 2.9 Fourth Amendment to Stock and Asset Purchase Agreement, dated as of November 30, 2001, by and among Rapid Link USA, Inc., Rapid Link Inc., and Dial Thru International Corporation. (filed as Exhibit 2.5 to the Company's Form 8-K dated December 28, 2001 and incorporated herein by reference)
- 2.10 Asset Purchase Agreement, dated as of October 25, 2005, by and between Integrated Communications, Inc. and Dial Thru International Corporation (filed as Exhibit 2.5 to the Company's Form 8-K dated October 31, 2005 and incorporated herein by reference)
- 3.1 Certificate of Incorporation, as amended (filed as Exhibit 3.1 to the Company's Annual Report on Form 10-K for the fiscal year ended October 31, 1999 (the "1999 Form 10-K") and incorporated herein by reference)
- 3.2 Amended and Restated Bylaws of Dial Thru International Corporation (filed as Exhibit 3.2 to the 1999 Form 10-K and incorporated herein by reference)
- 3.3 Amendment to Certificate of Incorporation dated January 11, 2005 and filed with the State of Delaware on January 13, 2005 (filed as Exhibit 3.3 to the 2004 Form 10-K and incorporated herein by reference)
- 3.4 Amendment to Certificate of Incorporation dated October 28, 2005 and filed with the State of Delaware on November 1, 2005
- 4.1 Securities Purchase Agreement issued January 28, 2002 between Dial Thru International Corporation and GCA Strategic Investment Fund Limited (filed as Exhibit 4.1 to the Company's Form S-3, File 333-82622, filed on February 12, 2002 and incorporated herein by reference)
- 4.2 Registration Rights Agreement dated January 28, 2002 between Dial Thru International Corporation and GCA Strategic Investment Fund Limited (filed as Exhibit 4.2 to the Company's Form S-3, File 333-82622, filed on February 12, 2002 and incorporated herein by reference)

## Edgar Filing: RAPID LINK INC - Form 10QSB

- 4.3 6% Convertible Debenture of Dial Thru International Corporation and GCA Strategic Investment Fund Limited (filed as Exhibit 4.3 to the Company's Form S-3, File 333-82622, filed on February 12, 2002 and incorporated herein by reference)
- 4.4 Common Stock Purchase Warrant dated January 28, 2002 between GCA Strategic Investment Fund Limited and Dial Thru International Corporation (filed as Exhibit 4.4 to the Company's Form S-3, File 333-82622, filed on February 12, 2002 and incorporated herein by reference)
- 4.5 Securities Purchase Agreement issued November 8, 2002 between Dial Thru International Corporation and Global Capital Funding Group, L.P. (filed as Exhibit 4.1 to the Company's Form 8-K filed on September 23, 2003, and incorporated herein by reference)
- 4.6 Secured Promissory Note issued November 8, 2002 between Dial Thru International Corporation and Global Capital Funding Group, L.P. (filed as Exhibit 4.2 to the Company's Form 8-K filed on September 23, 2003, and incorporated herein by reference)
- 4.7 Common Stock Purchase Warrant issued November 8, 2002 between Dial Thru International Corporation and Global Capital Funding Group, L.P. (filed as Exhibit 4.3 to the Company's Form 8-K filed on September 23, 2003, and incorporated herein by reference)
- 4.8 Registration Rights Agreement issued November 8, 2002 between Dial Thru International Corporation and Global Capital Funding Group, L.P. (filed as Exhibit 4.4 to the Company's Form 8-K filed on September 23, 2003, and incorporated herein by reference)
- 4.9 Securities Purchase Agreement issued July 24, 2003 between Dial Thru International Corporation and GCA Strategic Investment Fund Limited (filed as Exhibit 4.5 to the Company's Form 8-K filed on September 23, 2003, and incorporated herein by reference)
- 4.10 Promissory Note issued July 24, 2003 between Dial Thru International Corporation and GCA Strategic Investment Fund Limited (filed as Exhibit 4.6 to the Company's Form 8-K filed on September 23, 2003, and incorporated herein by reference)
- 4.11 Common Stock Purchase Warrant issued July 24, 2003 between Dial Thru International Corporation and GCA Strategic Investment Fund Limited (filed as Exhibit 4.6 to the Company's Form 8-K filed on September 23, 2003, and incorporated herein by reference)
- 4.12 Secured Promissory Note dated June 1, 2005 between Global Capital Funding Group, L.P. and Dial Thru International Corporation (filed as Exhibit 4.1 to the Company's Form 8-K filed on June 7, 2005, and incorporated herein by reference)
- 4.13 Common Stock Purchase Warrant dated June 1, 2005 between Global Capital Funding Group, L.P. and Dial Thru International Corporation (filed as Exhibit 4.2 to the Company's Form 8-K filed on June 7, 2005, and incorporated herein by reference)
- 4.14 Common Stock Purchase Warrant dated June 1, 2005 between Global Capital Funding Group, L.P. and Dial Thru International Corporation (filed as Exhibit 4.3 to the Company's Form 8-K filed on June 7, 2005, and incorporated herein by reference)

## Edgar Filing: RAPID LINK INC - Form 10QSB

- 4.15 Common Stock Purchase Warrant dated June 1, 2005 between GCA Strategic Investment Fund Limited and Dial Thru International Corporation (filed as Exhibit 4.5 to the Company's Form 8-K filed on June 7, 2005, and incorporated herein by reference)
- 4.16 Common Stock Purchase Warrant dated June 1, 2005 between GCA Strategic Investment Fund Limited and Dial Thru International Corporation (filed as Exhibit 4.6 to the Company's Form 8-K filed on June 7, 2005, and incorporated herein by reference)
- 4.17 Common Stock Purchase Warrant dated June 1, 2005 between GCA Strategic Investment Fund Limited and Dial Thru International Corporation (filed as Exhibit 4.7 to the Company's Form 8-K filed on June 7, 2005, and incorporated herein by reference)
- 10.1 Employment Agreement, dated June 30, 1997 between Canmax Retail Systems, Inc. and Roger Bryant (filed as Exhibit 10.3 to the Company's Registration Statement on Form S-3, File No. 333-33523 (the "Form S-3"), and incorporated herein by reference)
- 10.2 Commercial Lease Agreement between Jackson--Shaw/Jetstar Drive Tri-star Limited Partnership and the Company (filed as Exhibit 10.20 to the Company's Annual Report on Form 10-K dated October 31, 1998, and incorporated herein by reference)
- 10.3 Employment Agreement, dated November 2, 1999 between ARDIS Telecom & Technologies, Inc. and John Jenkins (filed as Exhibit 4.3 to the 2000 Form 10-K and incorporated herein by reference)
- 10.4 Amendment Number 1 to Securities Purchase Agreement dated June 1, 2005 between Global Capital Funding Group, L.P. and Dial Thru International Corporation (filed as Exhibit 10.1 to the Company's Form 8-K filed on June 7, 2005, and incorporated herein by reference)
- 10.5 Amendment Number 1 to Securities Purchase Agreement dated June 1, 2005 between GCA Strategic Investment Fund Limited and Dial Thru International Corporation (filed as Exhibit 10.2 to the Company's Form 8-K filed on June 7, 2005, and incorporated herein by reference)
- 10.6 Amendment Number 1 to Securities Purchase Agreement dated June 1, 2005 between GCA Strategic Investment Fund Limited and Dial Thru International Corporation (filed as Exhibit 10.3 to the Company's Form 8-K filed on June 7, 2005, and incorporated herein by reference)
- 14.1 Code of Business Conduct and Ethics for Employees, Executive Officers and Directors (filed as Exhibit 14.1 to the 2003 Form 10-K and incorporated herein by reference)
- 31.1 Certificate of Chief Executive Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934\*
- 31.2 Certificate of Chief Financial Officer pursuant to Rule 13a-14(a) and Rule 15d-14(a) of the Securities Exchange Act of 1934\*
- 32.1 Certificate of Chief Executive Officer pursuant to 18 U.S.C. Section 1350\*
- 32.2 Certificate of Chief Financial Officer pursuant to 18 U.S.C. Section 1350\*

\* Filed herewith.

Edgar Filing: RAPID LINK INC - Form 10QSB

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Rapid Link, Incorporated

By: /s/ John Jenkins

-----  
John Jenkins  
Chief Executive Officer

Dated June 14, 2006