

Company Registration No. 4287100

VTL (UK) Limited

Report and Financial Statements

31 December 2006

VTL (UK) Limited

Report and financial statements 2006

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VTL (UK) Limited

Officers and professional advisers

Directors

L Woods
S Blythe

Secretary

S Blythe

Registered office

Inbucon House
Wick Road
Egham
Surrey
TW20 0HR

Auditors

Deloitte & Touche LLP
Chartered Accountants
London

VTL (UK) Limited

Directors' report

The directors present the annual report and the audited financial statements for the year ended 31 December 2006.

Principal activity

The principal activity of the company is the provision of telecommunications services.

Review of developments and future prospects

The Company sells modern connectivity and IP networking products to Medium sized Enterprises (ME) in the UK. The product portfolio includes Broadband, Managed IPVPN, Hosting, Leased Lines and Voice over IP. Sales performance continues to be strong, with total revenue growth of 20% over the prior year, as the ME businesses in the UK embrace the latest communications technology. The directors anticipate that the revenues of the company will continue to grow significantly in the next year. Gross profit improved to 24% as compared with 14% for the prior year and cost management of administrative expenses also improved with a 22% reduction from the prior year.

To the extent that the company incurs liabilities to third parties it is dependent upon the continued financial support of its ultimate parent, Viatel Holding (Bermuda) Limited ("VHB"), to enable it to meet its debts as they fall due. As disclosed in the 2006 financial statements of VHB, which were filed with the US Securities and Exchange Commission (SEC), VHB is dependent upon the continued financial support of its investors to enable it to meet its obligations to both third parties and subsidiaries. VHB does not have sufficient funds to meet all of its forecast obligations for the next 12 months and is negotiating with its investors for further funding. Based on discussions with the directors of VHB, the directors have a reasonable expectation that VHB will receive adequate funding, based on the group's continued growth in revenues, improving financial performance and indications provided by investors regarding future financing. Accordingly, the directors of the company have prepared these accounts on a going concern basis. However, whether or not the investors will actually provide such funding represents a material uncertainty which casts significant doubt on the company's ability to continue as a going concern and it may be unable to realise its assets and discharge its liabilities in the normal course of business. The financial statements do not include any adjustments that would result if the going concern basis were not appropriate.

Subsequent to the year-end, the group received additional cash funding from its investors of £13.0 million to help support this growth.

Financial risk management objectives and policies

The company's activities expose it to a number of financial risks including credit risk and liquidity risk.

The company's principal financial assets are cash, trade and other receivables. The company's credit risk is primarily attributable to its trade receivables. The amounts presented in the balance sheet are net of allowances for doubtful receivables. The credit risk on liquid funds is limited because the counterparties are banks with high credit-ratings assigned by international credit-rating agencies. The company has no significant concentration of credit risk, with exposure spread over a large number of counterparties and customers. Additional information on the company's liquidity risks is given in note 1.

The group is not exposed to any material price or cash flow risks.

VTL (UK) Limited

Directors' report (continued)

Results and dividends

The company made a loss after taxation of £1,876,000 (2005: loss - £6,461,000). No dividends were proposed or paid during the year (2005: £nil).

Compliance with s234ZA of the Companies Act 1985

Each of the persons who is a director at the date of approval of this report confirms that:

- (1) so far as the director is aware, there is no relevant audit information of which the company's auditors are unaware; and
- (2) the director has taken all the steps that he/she ought to have taken as a director in order to make himself/herself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

This information is given and should be interpreted in accordance with the provisions of s234ZA of the Companies Act 1985.

Directors

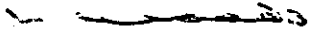
The directors who served the company throughout the year and since the year end are set out below:

L Woods
S Blythe

Auditors

Pursuant to s386 Companies Act 1985, an elective resolution was passed on 26 February 2004 dispensing with the requirement to appoint auditors annually. Therefore, Deloitte & Touche LLP are deemed to continue as auditors.

Approved by the Board of Directors
and signed on behalf of the Board


L Woods
Director

29 OCTOBER 2007

VTL (UK) Limited

Statement of directors' responsibilities

The directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with United Kingdom Generally Accepted Accounting Practice (United Kingdom Accounting Standards and applicable law). The financial statements are required by law to give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed; and
- prepare the financial statements on the going concern basis, unless it is inappropriate to presume that the company will continue in business.

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the company and to enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Independent auditors' report to the members of VTL (UK) Limited

We have audited the financial statements of VTL (UK) Limited for the year ended 31 December 2006 which comprise the profit and loss account, the balance sheet and the related notes 1 to 17. These financial statements have been prepared under the accounting policies set out therein.

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

Respective responsibilities of directors and auditors

The directors' responsibilities for preparing the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the Statement of Directors' Responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view in accordance with the relevant framework and are properly prepared in accordance with the Companies Act 1985. We also report to you whether in our opinion the information given in the Directors' Report is consistent with the financial statements.

In addition we report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the Directors' Report and consider the implications for our report if we become aware of any apparent misstatements within it.

Basis of audit opinion

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

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

Independent auditors' report to the members of VTL (UK) Limited (continued)

Opinion

In our opinion:

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2006 and of its loss for the year then ended; and
- the financial statements have been properly prepared in accordance with the Companies Act 1985; and
- the directors' report is consistent with the financial statements.

Emphasis of matter – Going concern

Without qualifying our opinion, we draw attention to the disclosures made in note 1 of the financial statements concerning the company's ability to continue as a going concern. The Company is dependent upon its ultimate parent company for financial support in order to enable it to meet its liabilities as and when they fall due. However, the ultimate parent company is in turn dependent on raising additional funds from its investors to continue as a going concern. These conditions, along with other matters set forth in note 1, indicate the existence of a material uncertainty which casts significant doubt about the company's ability to continue as a going concern. The financial statements do not include the adjustments that would result if the company was unable to continue as a going concern.

Deloitte & Touche LLP

Deloitte & Touche LLP
Chartered Accountants and Registered Auditors
London

30 October 2007

VTL (UK) Limited

Profit and loss account Year ended 31 December 2006

	Notes	2006 £'000	2005 £'000
Turnover	1	21,595	17,945
Cost of sales		(16,315)	(15,451)
Gross profit		<u>5,280</u>	<u>2,494</u>
Administrative expenses		(7,153)	(9,135)
Other operating income		-	202
Operating loss	2	<u>(1,873)</u>	<u>(6,439)</u>
Loss on disposal of tangible fixed asset		-	(45)
Interest receivable and similar income	5	111	49
Interest payable and similar charges	6	(114)	(26)
Loss on ordinary activities before taxation		<u>(1,876)</u>	<u>(6,461)</u>
Tax on ordinary activities	7	-	-
Loss on ordinary activities after taxation		<u>(1,876)</u>	<u>(6,461)</u>

There were no recognised gains or losses other than the loss for the current and prior years and therefore no statement of total recognised gains and losses has been presented.

All amounts relate to continuing activities.


VTL (UK) Limited

Balance sheet 31 December 2006

	Notes	2006 £'000	2005 £'000
Fixed assets			
Tangible fixed assets	8	4,194	4,264
Current assets			
Stocks – finished goods and goods for resale		89	70
Debtors	10	35,350	25,697
Cash		1,314	467
		<u>36,753</u>	<u>26,234</u>
Creditors: amounts falling due within one year	11	<u>(6,494)</u>	<u>(8,799)</u>
Net current assets		<u>30,259</u>	<u>17,435</u>
Total assets less current liabilities		<u>34,453</u>	<u>21,699</u>
Creditors: amounts falling due after more than one year	12	<u>(47,175)</u>	<u>(32,545)</u>
Net liabilities		<u>(12,722)</u>	<u>(10,846)</u>
Capital and reserves			
Called up share capital	13	18,000	18,000
Profit and loss account	14	<u>(30,722)</u>	<u>(28,846)</u>
Shareholder's deficit		<u>(12,722)</u>	<u>(10,846)</u>

These financial statements were approved by the Board of Directors on 29 October 2007.

Signed on behalf of the Board of Directors


L Woods
Director

VTL (UK) Limited

Notes to the accounts Year ended 31 December 2006

1. Accounting policies

The principal accounting policies are summarised below. They have been applied consistently throughout the current and prior years.

Basis of accounting

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

The company is not required to prepare consolidated accounts as it qualified as a medium-sized group under section 249 of the Companies Act 1985.

Cash flow statement and related party disclosures

The company is not required under FRS1 (Revised) to prepare a cash flow statement as the company is a wholly owned subsidiary of Viatel Holding (Bermuda) Limited which prepares consolidated accounts which are publicly available. The company is also exempt under FRS8 from disclosing transactions with other undertakings in the Viatel Holding (Bermuda) group.

Going concern

To the extent that the company incurs liabilities to third parties it is dependent upon the continued financial support of its ultimate parent, Viatel Holding (Bermuda) Limited ("VHB"), to enable it to meet its debts as they fall due. As disclosed in the 2006 financial statements of VHB, which were filed with the US Securities and Exchange Commission (SEC), VHB is dependent upon the continued financial support of its investors to enable it to meet its obligations to both third parties and subsidiaries. VHB does not have sufficient funds to meet all of its forecast obligations for the next 12 months and is negotiating with its investors for further funding. Based on discussions with the directors of VHB, the directors have a reasonable expectation that VHB will receive adequate funding, based on the group's continued growth in revenues, improving financial performance and indications provided by investors regarding future financing. Accordingly, the directors of the company have prepared these accounts on a going concern basis. However, whether or not the investors will actually provide such funding represents a material uncertainty which casts significant doubt on the company's ability to continue as a going concern and it may be unable to realise its assets and discharge its liabilities in the normal course of business. The financial statements do not include any adjustments that would result if the going concern basis were not appropriate.

Turnover

Turnover represents the invoiced value of services provided net of value added tax. Revenues are recognised on a pro-rata basis over the period of provision of service.

All turnover relates to the provision of service in the UK.

Foreign currencies

Transactions expressed in foreign currencies are translated into sterling and recorded at rates of exchange ruling at the date of the transaction. Monetary assets and liabilities are translated at rates ruling at the balance sheet date. Exchange differences are included in operating results.

VTL (UK) Limited

Notes to the accounts Year ended 31 December 2006

1. Accounting policies (continued)

Tangible fixed assets

Tangible fixed assets are stated at cost less accumulated depreciation and provision for impairment. Depreciation is provided on all tangible fixed assets other than freehold land, at rates calculated to write down the cost less estimated residual value, on a straight line basis over their expected useful lives. The rates applicable are:

Land and buildings	20 years (or lease term) straight line
Leasehold improvements	5 - 7 years straight line
Furniture and fittings	5 years straight line
Computer hardware	3 years straight line
Computer software	3 years straight line
Network infrastructure	3 - 20 years straight line

Leases

Assets held under finance leases and other similar contracts, which confer rights and obligations similar to those attached to owned assets, are capitalised as tangible fixed assets and are depreciated over the shorter of the lease terms and their useful lives. The capital elements of future lease obligations are recorded as liabilities, while the interest elements are charged to the profit and loss account over the period of the leases to produce a constant rate of charge on the balance of capital repayments outstanding.

Rentals under operating leases are charged on a straight-line basis over the lease term, even if the payments are not made on such a basis. Benefits received and receivable as an incentive to sign an operating lease are similarly spread on a straight-line basis over the lease term, except where the period to the review date on which the rent is first expected to be adjusted to the prevailing market rate is shorter than the full lease term, in which case the shorter period is used.

Pension costs

The group operates a defined contribution pension scheme. The amount charged to the profit and loss account in respect of pension costs and other post retirement benefits is the contributions payable in the year. Differences between contributions payable in the year and contributions actually paid are shown as either accruals or prepayments in the balance sheet.

Stocks

Stocks are stated at the lower of cost and net book value. Cost comprises amounts paid for materials. Net realisable value is based on estimated selling price less all relevant marketing, selling and distribution costs. Provision is made for obsolete, slow-moving or defective items where appropriate.

Taxation

Current tax is provided at amounts expected to be paid (or recovered) using the tax rates and laws that have been enacted or substantially enacted by the balance sheet date.

Deferred taxation is provided in full on all timing differences that result in an obligation at the balance sheet date to pay more tax, or a right to pay less tax, at a future date, at rates expected to apply when they crystallise based on current tax rates and law. Timing differences arise from the inclusion of items of income and expenditure in taxation computations in periods different from those in which they are included in financial statements. Deferred tax assets and liabilities are not discounted.

VTL (UK) Limited

Notes to the accounts (continued) Year ended 31 December 2006

2. Operating loss

	2006 £'000	2005 £'000
The operating loss is stated after charging:		
Depreciation	1,300	996
Impairment of fixed assets	-	150
Amounts paid under operating leases for land and buildings	697	760

Auditor's remuneration

	2006 £'000	2005 £'000
Fees payable to the company's auditors for the audit of the company's annual accounts.	45	45
Fees payable to the company's auditors and their associates for other services to the group:		
The audit of fellow group companies	215	198
<i>Total audit fees</i>	<u>260</u>	<u>243</u>
Tax services	35	29
<i>Total non-audit fees</i>	<u>35</u>	<u>29</u>

The amount shown as auditors' remuneration is that attributable to the audit of VTL UK. VTL UK incurred the full cost of audit services performed for the Viatel group on behalf of the ultimate parent company, Viatel Holding (Bermuda) Limited.

3. Staff costs

	2006 £'000	2005 £'000
Staff costs were as follows (including directors):		
Wages and salaries	6,827	9,273
Social security costs	806	994
Other pension costs	260	427
	<u>7,893</u>	<u>10,694</u>

VTL (UK) Limited

Notes to the accounts (continued) Year ended 31 December 2006

3. Staff costs (continued)

	2006 No.	2005 No.
The monthly average number of employees, including directors during the year was as follows:		
Management and administration	19	17
Sales support and marketing	82	86
Technical	48	42
	<u>149</u>	<u>145</u>

4. Directors' emoluments

The directors received £nil (2005: £nil) during the year in respect of services to the company. The directors are also directors of other group undertakings and their remuneration was incurred by VHB. It is not practicable to allocate their remuneration to specific group undertakings.

5. Interest receivable and similar income

	2006 £'000	2005 £'000
Bank interest receivable	40	22
Interest receivable from group undertakings	71	27
	<u>111</u>	<u>49</u>

6. Interest payable and similar charges

	2006 £	2005 £
Bank interest payable	104	26
Finance charge arising on discounted liabilities	10	-
	<u>114</u>	<u>26</u>

VTL (UK) Limited

Notes to the accounts (continued) Year ended 31 December 2006

7. Tax on ordinary activities

(i) Factors affecting tax charge for the current year.

The tax assessed for the year is higher than that resulting from applying the standard rate of corporation tax in the UK: 30% (2005: 30%).

The differences are explained below:

	2006 £'000	2005 £'000
Loss on ordinary activities before tax	(1,876)	(6,461)
Tax at 30% thereon:	563	1,938
Effects of:		
Expenses not deductible for tax purposes	(210)	(299)
Capital allowances less than depreciation	(390)	(357)
Utilisation of brought forward losses	42	(1,175)
Movement in short term timing differences	(5)	(107)
Current tax charge for year	-	-

(ii) Factors that may affect the future tax charge

A deferred tax asset has not been recognised in respect of tax losses carried forward, fixed asset timing differences and other timing differences as there is insufficient evidence that the asset will be recovered. The asset would be recovered if sufficient profits arose in the future against which the asset could be offset. The amounts of the asset not recognised are:

	2006 £'000	2005 £'000
Tax losses carried forward	3,788	3,855
Fixed asset timing differences	1,029	731
Other timing differences	186	182
	5,003	4,768

VTL (UK) Limited

Notes to the accounts (continued) Year ended 31 December 2006

8. Tangible fixed assets

	Land and buildings £'000	Leasehold impro- vements £'000	Furniture and fixtures £'000	Computer hardware £'000	Computer software £'000	Network infra- structure £'000	Total £'000
Cost							
As at 1 January 2006	290	379	44	711	751	4,613	6,788
Additions	-	199	3	246	189	593	1,230
As at 31 December 2006	290	578	47	957	940	5,206	8,018
Depreciation							
As at 1 January 2006	121	147	21	434	396	1,405	2,524
Charge for the year	32	74	9	215	154	816	1,300
As at 31 December 2006	153	221	30	649	550	2,221	3,824
Net book value							
As at 31 December 2006	137	357	17	308	390	2,985	4,194
As at 31 December 2005	169	232	23	277	355	3,208	4,264

9. Fixed asset investments

The company has investments in the following subsidiary undertaking.

Subsidiary undertakings	Place of registration	Principal activity	% held
Viatel Internet Limited	England and Wales	Network Services	100
			2006
			£'000
Cost at 1 January 2006 and 31 December 2006			2,011
Net book value at 1 January 2006 and 31 December 2006			-

Viatel Internet Limited made a loss of £104,000 for the year ended 31 December 2006 and its aggregate capital and reserves as 31 December 2006 were a deficit of £2,105,000.

10. Debtors

	2006 £'000	2005 £'000
Trade debtors	1,566	1,067
Amounts owed by group undertakings	29,378	22,929
Other debtors	510	809
Prepayments and accrued income	3,896	892
	35,350	25,697

VTL (UK) Limited

Notes to the accounts (continued) Year ended 31 December 2006

11. Creditors: amounts falling due within one year

	2006 £'000	2005 £'000
Bank loans and overdrafts	-	4,053
Trade creditors	3,420	2,141
Other taxation and social security	757	497
Other creditors	445	155
Accruals and deferred income	1,872	1,953
	<u>6,494</u>	<u>8,799</u>

12. Creditors: amounts falling due after more than one year

	2006 £'000	2005 £'000
Amounts owed to group undertakings	45,501	32,545
Accruals and deferred income	1,674	-
	<u>47,175</u>	<u>32,545</u>

In April 2004 amounts due to group undertakings were refinanced through the group downstream facility. All amounts are due to be repaid in April 2013 but may be repaid at the borrower's option before then. These amounts are subordinated to the claims of all other creditors. As a result of entering into the financing arrangement, the assets of the company have been provided as security to the holders of the financing.

13. Called up share capital

	2006 £	2005 £
Authorised:		
18,500,000 (2005: 18,500,000) ordinary shares of £1 each	<u>18,500,000</u>	<u>18,500,000</u>
Allotted, called up and fully unpaid:		
18,000,001 (2005: 18,000,001) ordinary shares of £1	<u>18,000,001</u>	<u>18,000,001</u>

14. Reconciliation of movement in shareholder's deficit

	Called up ordinary share capital £'000	Profit and loss account £'000	Total equity shareholder's deficit £'000
At 1 January 2006	18,000	(28,846)	(10,846)
Loss for the financial year	-	(1,876)	(1,876)
At 31 December 2006	<u>18,000</u>	<u>(30,722)</u>	<u>(12,722)</u>

VTL (UK) Limited

Notes to the accounts (continued) Year ended 31 December 2006

15. Annual commitments under non cancellable operating leases are as follows

	Land and buildings	
	2006	2005
	£'000	£'000
Expiry date		
- within one year	20	63
- between two and five years	48	227
- after five years	434	434
	<hr/>	<hr/>
	502	724
	<hr/>	<hr/>

In the normal course of business, the company has entered into contracts to procure internet connectivity, some of which have minimum purchase levels. As at the year end, the company has an obligation to purchase £550,000 of capacity in the next 12 months.

16. Ultimate parent undertaking and controlling party

The directors consider Morgan Stanley, a company incorporated in the United States, to be the ultimate controlling party. The ultimate parent undertaking is VHB and this is the only group in which the company is consolidated. Copies of the group accounts can be obtained from Viatel Holding (Bermuda) Limited at Inbucon House, Wick Road, Egham, Surrey, TW20 0HR.

The immediate parent undertaking is VTL Inc, a company incorporated in the United States.

17. Related party transactions

Morgan Stanley, the ultimate controlling party, has guaranteed a bank facility of VTL (UK) Ltd. This guarantee was in force at 31 December 2005 and had a maximum limit of £5.8 million. The guarantee was backed by an additional charge on the assets of the company. The bank facility was repaid and cancelled on the 7th April 2006.

During 2006 the company paid £394,000 (2005 :£378,000) of emoluments to Lucy Woods, a director of VTL (UK) Ltd, but these were recharged to VHB as they relate entirely to services provided to that entity.

During 2006 the company paid £231,000 (2005: £220,000) of emoluments to Stuart Blythe, a director of VTL (UK) Ltd, but these were recharged to VHB as they relate entirely to services provided to that entity.

VHB has outstanding loan notes of \$102.8million (2005: \$73.6million) which are secured on the assets of the company and fellow group undertakings. At 31 December 2006, \$74.3million (2005: \$52.3million) was due to Morgan Stanley and \$583,000 (2005: \$276,000) was due to Lucy Woods. The balance is due to third parties.