



Management's Discussion and Analysis

Year ended December 31, 2005

This document provides management's discussion and analysis (MD&A) of our financial condition and results of operations for the year ended December 31, 2005, compared to 2004. The MD&A should be read in conjunction with our consolidated financial statements and accompanying notes for the year ended December 31, 2005. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (Canadian GAAP). All amounts in this MD&A are in millions of Canadian dollars, except where otherwise noted.

Throughout this MD&A, "we", "us", "our" and "Aliant" refer to Aliant Inc. or our telecommunications and information technology segments.

Quarterly and annual reports and supplementary financial information can be found under "Financial reports" on our corporate website at www.aliant.ca. Quarterly and annual reports, annual information forms and other continuous disclosure documents have been filed electronically through the System for Electronic Document Analysis and Retrieval and are available online at www.sedar.com.

This MD&A is dated January 26, 2006, and is current to that date, unless otherwise stated. This document contains forward-looking statements, which are qualified by reference to, and should be read together with, the "Forward-looking statements" section.

Restatement of prior year results

Effective January 1, 2005, we changed our accounting policies for subscriber acquisition costs and for the recognition of revenues and expenses in our directory business. These changes have been applied retroactively with restatement of prior periods.

About our business

Who we are

We are Atlantic Canada's leading information and communications technology (ICT) provider, complementing our telecommunications business with strengths in information technology to deliver complete customer solutions. We are listed on the Toronto Stock Exchange (TSX) and are the largest publicly traded company based in Atlantic Canada.

We have more than 100 years of experience in traditional communications services and have the knowledge and experience to help organizations make information technology (IT) a valuable and responsive tool. We are focused on combining these strengths to be the provider of choice

for all communications, information and entertainment services. We offer simple world-class solutions that meet the needs of our customers in Atlantic Canada and other regions, and deliver them in a way which makes us easy to do business with. We listen to and collaborate with our customers and other partners to ensure we are on the leading edge of information and communications technology. We combine the dependability and quality of our infrastructure, innovation and customer service to enhance the capabilities of our customers.

What we do

Our telecommunications segment is primarily carried out by our subsidiary, Aliant Telecom Inc. We provide a wide range of innovative and traditional voice and data communications services including local, long distance, wireless, Internet and other services. We also have wholly owned subsidiaries that provide complementary services in knowledge management, including e-learning, technical documentation and tele-web sales and service, offered through Innovatia Inc. (Innovatia), and retail sales through our Aliant dealer and communications outlets located throughout Atlantic Canada and provided through DownEast Ltd. (DownEast). In addition, we maintain an 87.1 per cent joint venture interest in Aliant ActiMedia, which produces and distributes telephone directories in our region, and we offer wholesale distribution of wireless handsets, accessories and other telecommunications products through our 45.0 per cent ownership interest in Atlantic Mobility Products Ltd.

Our information technology segment is carried out through Xwave Solutions Inc. (xwave). xwave is a full-service business solutions provider that serves clients through systems integration, infrastructure services and fulfillment.

Throughout 2005, we have aggressively continued the convergence of our telecommunications and information technology segments such that specialized expertise and common sales, marketing and customer service channels allow us to offer complete ICT solutions for our customers. We serve clients in several geographic markets and across many different industries.

Our business environment

The communications industry continues its rapid transformation. The convergence of the telecommunications industry with the broadcast television distribution and IT industries is resulting in new customer solutions, new opportunities and new competition. Atlantic Canada remains one of the most competitive markets in the country for local service, and competition across all areas of our business is intensifying. Technological evolution is creating a world in which data, video and voice share a common Internet protocol (IP)-based communication platform. By sharpening our focus as an ICT company, we can use complementary technologies to build on existing core network components of access and connectivity. In addition to our telecommunications services, we offer managed network and hosted services and applications and we can deliver even greater customer value through integration and consulting services. We have the ability to keep pace with the current rapid rate of technological change while ensuring that solutions work for customers and that our networks remain reliable.

To remain competitive in this evolving communications industry, we plan to invest heavily in growth areas of our business while maintaining reliable core networks. We will also continue to

simplify and enhance the customer experience, and transform our cost structure through expense management and productivity improvements.

Regulatory environment

The business of our telecommunications segment is affected by regulatory decisions made by the Canadian Radio-television and Telecommunications Commission (“CRTC” or the “Commission”). The regulatory environment was challenging in 2005, with several decisions that will have significant consequences for the telecommunications industry and could negatively affect our revenues, profitability and competitive position.

- In February 2005, the CRTC issued its competitor digital network (CDN) decision, which established how incumbent local exchange carriers (ILECs) are to provide digital network services to their competitors. The decision resulted in our competitors paying much less for some of our services. The negative impact on our revenues in 2005 as a result of this decision was \$12.0 million.
- In March 2005, the CRTC issued its decision regarding Quality of Service rebates applicable to retail services if ILECs do not meet minimum service standards. We did not meet certain of these service standards during 2004 due to the labour disruption. We have filed an application with the CRTC to request the exclusion of certain results from the Quality of Service rebate calculations. We anticipate a ruling on our application in early 2006.
- In May 2005, the CRTC indicated that Voice over Internet Protocol (VoIP) services will be regulated in a manner similar to regulated local telephone service. In conjunction with other Canadian ILECs, we filed a petition with the Governor in Council requesting that the decision be reviewed and overturned in the spirit of innovation and competition in Canada.
- In December 2005, the CRTC issued its decision on the implementation of Wireless Number Portability, providing for the porting of telephone numbers between wireless carriers in Canada, and between wireless and wireline services.

In addition, we expect the CRTC to issue decisions in 2006 on our application for forbearance from price regulation of local residential services in certain areas of Nova Scotia and Prince Edward Island, and on the amount and distribution of money in deferral accounts that were established pursuant to the 2002 Price Cap Decision.

Further details of our regulatory risks are identified in the “Risk and risk management” section.

Year at a glance

Financial results

For the years ended December 31

(millions of dollars, except per share amounts)

| | 2005 | 2004 | % change |
|---------------------------|------------|------------|----------|
| Operating revenues | \$ 2,096.7 | \$ 2,033.5 | 3.1 |
| Expenses | 1,701.8 | 1,763.9 | (3.5) |
| Operating income | 394.9 | 269.6 | 46.5 |
| Other income (expenses) | (3.2) | 4.3 | - |
| Interest charges | 73.8 | 75.0 | (1.7) |
| Income taxes | 116.0 | 66.4 | 74.6 |
| Non-controlling interest | 2.5 | 1.8 | 43.5 |
| Net income | \$ 199.4 | \$ 130.7 | 52.6 |
| Earnings per common share | \$1.46 | \$0.91 | 60.4 |

Operating revenues for 2005 increased by 3.1 per cent over the prior year fuelled by strong fourth quarter growth of 4.9 per cent and a full recovery from the labour disruption in 2004. Growth was achieved in all areas, except in traditional local and long distance services.

- Wireless revenue grew 13.8 per cent over 2004 driven by an 11.9 per cent increase in our customer base and a 4.0 per cent increase in average revenue per customer (ARPC).
- Internet revenue grew 10.7 per cent for the year, driven by year-over-year high-speed Internet customer growth of 41.8 per cent and high-speed Internet revenue growth of 24.5 per cent.
- Telecommunications product revenues increased 13.4 per cent over 2004, reflecting our recovery from the sales slowdown that arose during the 2004 work stoppage.
- IT service revenue for 2005 experienced growth of 10.5 per cent, excluding the impact of 2004 divestiture activity. The impact of an acquisition in late 2004 and organic growth through new contracts contributed to the increase.
- IT fulfillment revenue grew by 5.3 per cent, with growth reflective of a strong economy driving healthy business spending.
- Revenues from our local and long distance services continued to decline, but the decline has slowed in recent quarters. Declining revenue trends are due to competition, technology substitution and regulatory constraints. The February 2005 CRTC ruling on CDN service negatively affected our local revenues by \$12.0 million in 2005.

Operating income for 2005 increased by 46.5 per cent over 2004. The improvement was driven by the strong recovery from the 2004 labour disruption, somewhat offset by the impact of the CRTC's CDN decision and an increase in pension and other post-employment benefits (OPEBs) costs. We remain satisfied that operating expense increases required to drive revenue growth

are being contained through expense management and productivity improvements, including the savings achieved from the early retirement incentive program (ERIP) implemented in late 2004. We estimate that the departure throughout 2005 of the 693 employees who accepted the voluntary offer removed approximately \$39 million in operating expenses for 2005.

We generated cash from operating activities of \$524.3 million in 2005, within our guidance range provided for the year, but 8.9 per cent lower than operating cash generated in 2004. Growth in cash earnings was offset by higher required defined benefit (DB) pension plan contributions and lower cash from changes in working capital. Strong operating cash flows facilitated the execution of our strategic priorities for the year. During 2005, we spent \$363.2 million on capital investments, primarily focused on next-generation infrastructure, to support our strategy of growth and transformation.

Performance measured against 2005 guidance

| <i>(millions of dollars, except earnings per share amounts)</i> | 2005 results | 2005 guidance | Met ✓ Not met ✕ |
|---|---------------------|----------------------|----------------------------------|
| Operating revenues | \$2,097 | \$2,080 to \$2,120 | ✓ |
| Earnings per share | \$1.46 | \$1.35 to \$1.42 | ✓ |
| Cash from operating activities | \$524 | \$510 to \$560 | ✓ |
| Capital investments ¹ | \$363 | \$330 to \$370 | ✓ |

¹Capital investments exclude assets acquired through capital leases totalling \$12.0 million.

Our 2005 operating revenues, cash from operating activities and capital investments were within our guidance ranges. Our earnings per share exceeded the guidance we issued.

Delivered shareholder returns

During 2005, we delivered value to our shareholders through the declaration of dividends amounting to \$1.18 per common share, an increase of 7.3 per cent over 2004. As well, excess cash of \$161.4 million was returned to shareholders through our normal course issuer bid (NCIB), as we purchased for cancellation 5,797,715 common shares.

Strategic accomplishments in 2005

During the fourth quarter of 2005, the execution of our growth and transformation strategy resulted in the advancement of many of our ongoing initiatives and the achievement of several significant accomplishments:

- Success of our holiday marketing programs and our very popular PC purchase program, within our value packages, contributed to Internet revenue growth of 20.0 per cent for the quarter compared to the same period in 2004. This demonstrates excellent progress toward our goal to “own” the broadband home.
- We launched Aliant IP virtual private network (VPN), our next generation business IP wide-area network (WAN) data service, connecting customers’ offices and data centres throughout Atlantic Canada to the rest of the country. This service enhances our ability to provide ICT solutions that add value and efficiencies to our customers’ businesses.

Aliant IP-VPN is the first IP service to be offered by us over our new state-of-the-art national multi-protocol label switching (MPLS) network, developed along with Bell Canada. MPLS is an underlying networking technology that enables us to deliver VoIP, IP video conferencing, IP call centre applications and other future IP applications.

- xwave signed a multi-million dollar contract with General Dynamics Canada, part of the Sikorsky Aircraft-led Maritime Helicopter Team, to develop ground-based simulators and software in support of Canada's new CH148 Cyclone helicopters.
- We launched our wireless fleet and asset management solutions, including automatic vehicle location, which utilizes global positioning satellite technology and the integration of wireless communications, vehicle monitoring systems and location devices.
- We launched a technology trial and our plans to roll out Evolution Data Optimized (EV-DO), a third generation (3G) digital wireless technology. Aliant's EV-DO service will initially be introduced to customers in the Halifax area in early 2006 and then expanded to other areas across Atlantic Canada.

Throughout the year, we have provided updates on our progress against our seven strategic initiatives. The following table provides a snapshot of some of our key accomplishments for 2005.

| Strategic initiative | Notable achievements during 2005 |
|---|---|
| Capture new growth and defend existing revenues by “owning” the broadband home. | <ul style="list-style-type: none"> ✓ We expanded our high-speed Internet footprint by adding 502 sites and upgrading 118 of our existing sites. ✓ We significantly increased our value package penetration by simplifying pricing and introducing new services and features. ✓ We launched Aliant TV and have experienced steady growth in homes passed and our number of customers. |
| Become the most trusted ICT advisor to the small-to medium-sized business (SMB) market. | <ul style="list-style-type: none"> ✓ We built an ICT service delivery and support model that ensures a positive customer experience. We educated customers through our Aliant Business Solutions stores, education road shows and an “ICT awareness” campaign. ✓ We launched several new services and solutions for the SMB market, including integrated solutions designed for key industry verticals. ✓ We expanded our distribution channels through several new value-added resellers. |

| | |
|--|--|
| <p>Serve the enterprise market by innovating with customers.</p> | <ul style="list-style-type: none"> ✓ We launched Aliant IP-VPN, our next-generation business IP WAN data service connecting customers' offices and data centres throughout Atlantic Canada and across the country. ✓ We integrated functions of our information technology segment into our telecommunications segment, which allowed us to align people, processes, systems and tools to more efficiently develop and deliver ICT solutions. ✓ We designed innovative solutions for our customers, which led to several contracts for Canada's Maritime Helicopter Project totalling more than \$200 million, including a 20 year contract with L-3 Communications MAS (Canada) Inc. for the design, provision and long-term support of the integrated information environment. We also signed a contract with General Dynamics Canada to develop ground-based simulators and software. Another innovative solution we designed in 2005 was a clinical management system for Ontario physicians, which led to a 15 year contract with a subsidiary of the Ontario Medical Association. |
| <p>Innovate with customers to drive growth through new technologies and enhanced customer experiences.</p> | <ul style="list-style-type: none"> ✓ We performed technology trials throughout the year with various user-groups as we work to develop and refine our VoIP platforms. ✓ We opened the Bell-Aliant SMB Innovation Centre, a state-of-the-art research and development facility where IP-based applications for the national SMB market are being created and tested. ✓ We launched a technology trial and plans to roll out EV-DO wireless technology. ✓ We launched Aliant ethernet service, delivering higher quality voice and data feeds over a single access in a cost-effective manner. |
| <p>Redefine the way we work to better serve our customers, reduce costs and safeguard our future.</p> | <ul style="list-style-type: none"> ✓ We transformed parts of our customer service operations through the creation of customer contact centres of excellence and enhanced self-serve tools available to our customers on Aliant.net. ✓ We advanced in our e-billing strategy with the launch of and conversion to e-billing solutions for certain customers. ✓ We implemented productivity and cost management initiatives across all segments of our business. |
| <p>Transform our business model by accelerating adoption of IP technology.</p> | <ul style="list-style-type: none"> ✓ In conjunction with Bell Canada, we developed our new state-of-the-art MPLS network, which enables us to deliver VoIP and other IP applications. ✓ We invested in Aliant TV, VoIP and Internet-enabled wireless applications. ✓ We continued to expand and enhance the capabilities of our broadband and digital wireless data networks. |
| <p>Invest in new skills required to grow and transform our business.</p> | <ul style="list-style-type: none"> ✓ We took a major step toward transforming our operations and cost structure through the departure of 693 employees under the ERIP offered in late 2004. ✓ We developed comprehensive learning strategies and resource planning initiatives, which will support our employees as their roles evolve through the transformation of our business. |

2006 strategic direction

Growth and transformation strategy

In order to compete more effectively, in 2005 we embarked on a strategy of growth and transformation by adopting new products and technologies to grow our revenues and by transforming our existing business structure. In 2006, we will accelerate the pace of our growth and transformation strategy as we strive to be the premier ICT company in Atlantic Canada and the provider of choice for our customers' information, communications and entertainment services.

Our **growth** strategy continues to be developed around our objectives to “own” the broadband home, to serve the enterprise market in key ICT verticals and to become the trusted advisor to the SMB market.

Residential growth

Value package penetration will continue to be the key to our success in the residential market. Value packages allow us to maximize the profitability of our traditional voice services and position us for growth in newer services by securing a loyal customer base. In 2006, we plan to strengthen and differentiate our value packages through new and unique products and superior customer service. We will improve our delivery of value packages by simplifying and improving the customer buying and billing experience. We will also continue to invest in the growth areas of wireless, Internet and IP-TV to ensure that we have the right services in the future to be the provider of choice for Atlantic Canadian residential customers.

Enterprise growth

In 2006 and beyond, we expect the traditional boundaries between telecommunications and IT to further erode. Our strategy is built on positioning us to offer fully integrated solutions to our customers in Atlantic Canada and adjacent markets. We will promote service delivery excellence through a single point of contact for ICT solutions and we will innovate with our customers to develop new solutions, particularly within key ICT verticals such as health care, government and public defence, where our expertise has allowed us to become a trusted leader. We also intend to leverage our strengths as we lead our customers through their transition to next generation IP services.

SMB growth

We plan to continue raising awareness amongst our SMB customers of the benefits that ICT solutions can bring to their businesses. We plan to continue developing ICT solutions to meet the needs of this broad market. In 2006, we will continue to enhance and promote our business bundles in order to foster customer loyalty and retention. We will simplify the SMB customer experience through a single point of contact for all inbound calls, increased training for our front line employees, and expanded online tools and self-serve solutions.

Our **transformation** strategy will continue in 2006 as our core network evolves to enable new IP-based services and as we transform operations and productivity to create a next generation cost structure for our business.

Network transformation

In 2006, we plan to expand the national multi-service IP core network to enable new IP-based services and meet customer demand. We will be transforming our cellular network into a high-speed data network through the deployment of 3G EV-DO digital wireless technology. We will be accelerating the replacement of copper-based technology with fibre systems and, in some areas, implementing performance improvement solutions for existing copper-based technology.

Operations transformation

We plan to simplify and enhance our customer experience in 2006 through the redesign of internal processes and the introduction of new systems and tools. We will continue our billing transformation by aligning our billing systems to facilitate e-billing and the consolidation and simplification of bills.

Productivity and cost structure improvements will primarily be gained through process improvement and increased discretionary spending controls. We also plan to evaluate outsourcing opportunities and we have redesigned our OPEBs to make this cost more controllable in the future.

2006 Financial outlook

In 2006, we expect to achieve revenue growth from our high-speed Internet and digital wireless services and to capture more of the ICT market in Atlantic Canada and adjacent geographies, but see continued, albeit slower, declines in local and long distance revenues.

We will strive to preserve local and long distance revenues by emphasizing enhanced functionality and superior quality, and by leveraging our value packages and business bundles. Wireless growth will focus on delivering quality product performance and customer service to our existing and new customer base. We will increase data revenue by launching 3G EV-DO digital wireless technology, targeting 60 per cent coverage of Atlantic Canadians by the end of 2007. The Internet business is increasingly important due to the IP-based nature of next generation networks and associated applications. We plan to grow Internet revenue by modestly expanding our high-speed Internet footprint, increasing broadband service adoption by existing customers and attracting new customers through the promotion of our value packages and unique services, such as security solutions, ultra high-speed, dedicated access and aliant.net.

IT revenues are expected to increase as we leverage our ICT integration and introduce new ICT solutions for key industries, such as contact centres, health care and the public sector.

We anticipate increased net income from revenue growth and through productivity improvements. We also expect to benefit from an effective tax rate that remains consistent with Canadian statutory rates. However, our net income for 2006 is expected to be negatively affected by the accounting for non-cash losses on two interest rate swaption contracts that we anticipate will be exercised during 2006. For details on these contracts and the anticipated outcomes, refer to the “Other financial arrangements” section.

Our balance sheet remains strong and we anticipate generating more than sufficient cash flow in 2006 to meet our operating, financing and investing requirements. Our total pension plan contributions for 2006 are estimated at \$120 million to \$130 million. These estimates include our anticipated impact of lower interest rates that were in effect at the end of 2005 and new actuarial valuation rules that were enacted in the last year, however, they are subject to revision based on new plan valuations to be completed later in 2006.

We intend to renew our NCIB after the expiry of the current NCIB in February 2006. In addition, we have declared a common share dividend for the first quarter of 2006 at the rate of \$0.31 per common share, representing a 5.1 per cent increase over the dividend declared for the same period in 2005. We will also continue to make capital investments and meet our contractual obligations.

In 2006, our capital investments will reflect a continued emphasis on strategic initiatives required to grow and transform our business. Being aggressive in our pursuit of new growth involves capital investment to support evolution of our IP networks and applications, expanding the capability and reach of our broadband and wireless networks, and ensuring the capacity to support customer commitments and growth in all areas of our business. Approximately 60 per cent of our 2006 capital investments will support continued growth in our business.

As our traditional business changes, we are aggressively transforming our cost structure and the way in which we serve our customers. Our planned 2006 investments support ongoing programs which improve the ability of our front line staff and dealers to serve customers, add new capability to our billing platforms, expand self-serve access for our customers, and drive operational effectiveness and productivity improvements across all facets of our business. Approximately 20 per cent of our 2006 capital investments will support improving our customer experience and transforming our operational effectiveness.

Reliable service is of critical importance to our customers. In 2006, we will continue to invest in the replacement of existing networks, infrastructure, real estate, vehicles and tools to ensure we are able to maintain the highest levels of reliability. Approximately 20 per cent of our 2006 capital investments will be directed toward sustaining our existing business and levels of reliability.

Operating results

The following is our discussion and analysis of the significant components of our consolidated operating results for year ended December 31, 2005, in comparison to the prior year.

Operating revenues

For the years ended December 31

(millions of dollars)

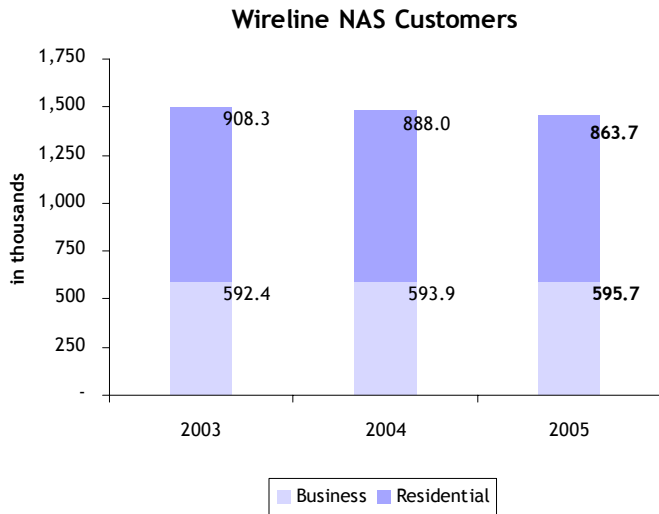
| | 2005 | 2004 | % change |
|-------------------------------------|-------------------|-------------------|------------|
| Telecommunications | | | |
| Local | \$ 728.3 | \$ 750.2 | (2.9) |
| Long distance | 318.9 | 348.5 | (8.5) |
| Wireless | 439.6 | 386.4 | 13.8 |
| Internet | 131.9 | 119.1 | 10.7 |
| Other revenues | 233.9 | 197.9 | 18.2 |
| | 1,852.6 | 1,802.1 | 2.8 |
| Information Technology | | | |
| IT Services | 205.1 | 200.6 | 2.2 |
| Fulfillment | 150.5 | 142.9 | 5.3 |
| | 355.6 | 343.5 | 3.5 |
| Other and intercompany eliminations | (111.5) | (112.1) | (0.5) |
| Operating revenues | \$ 2,096.7 | \$ 2,033.5 | 3.1 |

Local revenue

Local revenue is earned through providing the following services to residential and business customers:

- Network access service (NAS) - monthly access charges for provision of local telephone service;
- Enhanced service features - value added services such as call answer, call display and call forwarding;
- Data access - consists of local data access services, such as frame relay, asynchronous transfer mode and interoffice digital access;
- Contribution payments - subsidies from the telecommunications industry-financed National Contribution Fund for the provision of residential local service in high cost areas;
- Competitor payments - fees paid by competitors that access our local network; and
- Other revenues - from telephone set rentals, payphone usage and service charges.

Local revenues in 2005 were 2.9 per cent lower than 2004 due to competition, technology substitution, regulatory decisions rendered during the year and continued regulatory restriction.



The majority of our local revenues are earned through the provision of NAS. NAS revenues declined by 0.8 per cent in 2005 due to a 1.5 per cent decline in our NAS customer base compared to last year. Our residential NAS customers declined by 2.7 per cent, which represents competitive losses, the reduction in the number of second lines as dial-up customers migrate to high-speed Internet service and a reduction in primary lines as customers adopt wireless and VoIP technology. Partially mitigating the NAS revenue decline were modest increases in business prices implemented in December 2004, combined with a slight increase in

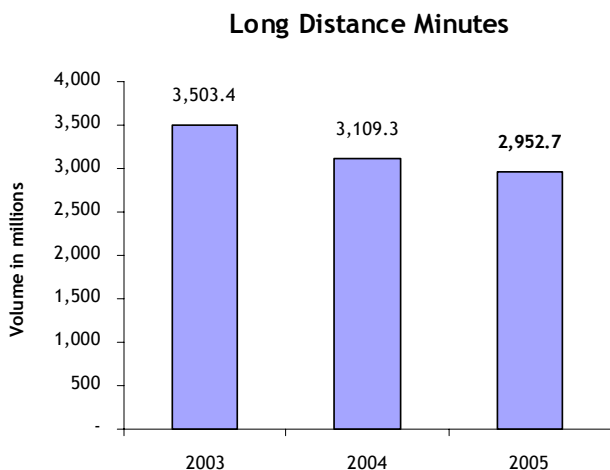
business NAS customers driven by marketing programs that support customer retention and growth.

Revenue from sources other than NAS, declined by 6.1 per cent in 2005. Growth in data access services was offset by a \$12.0 million impact of the CRTC's CDN decision, which required us to charge lower wholesale prices to our competitors. Enhanced service features revenue for the year declined 5.7 per cent due to declines in residential NAS customers and lower pay-per-use revenues as customers adopt features inside our local service value packages. Telephone set rental revenue declined 11.8 per cent as customers are increasingly opting to purchase sets rather than rent.

Long distance revenue

Long distance revenue is earned through providing the following services to residential and business customers:

- Toll service - long distance voice services, including toll-free service;
- Data network service - long distance data transmission circuits; and
- Long distance terminating - the rates paid by certain telecommunications carriers for long distance calls terminating with our customers.



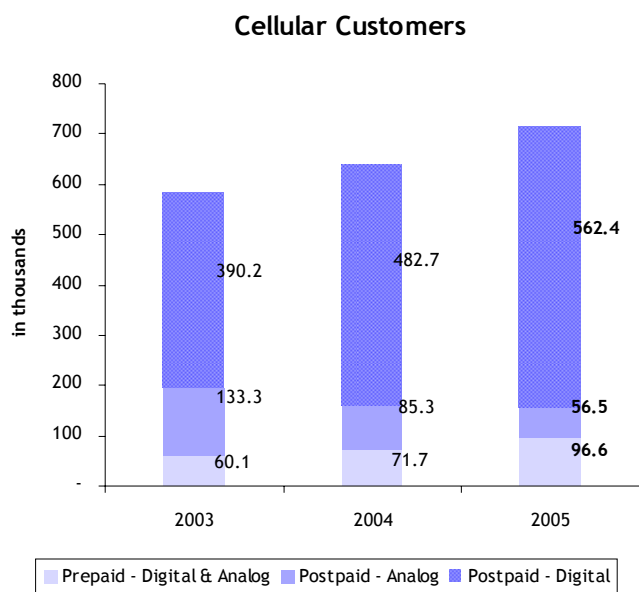
Long distance revenues for 2005 declined 8.5 per cent from 2004 as a result of lower per-minute pricing and a 5.0 per cent decline in long distance minutes.

Business long distance revenues declined 10.7 per cent due to competitive pricing pressure and contact centre minute usage reductions, as the contact centre industry progresses in its evolution to IP-based technologies.

Residential long distance declined 8.7 per cent due to intense competition, particularly from dial around competitors and from minute erosion caused by substitution of wireline long distance with wireless and Internet communications. Our residential customer base stabilized in 2005 through the successful promotion of long distance plans offered in our value packages. The conversion of customers to our value packages contributes to lower pricing allocations to our long distance revenue but secures our customer base for marketing our wireless and Internet services and mitigates future price declines through the use of fixed monthly prices.

Wireless revenue

Wireless revenue is earned through the provision of cellular, paging and mobile radio services over our analog and digital wireless network. Cellular revenues consist primarily of monthly recurring charges and also include charges for airtime, long distance, roaming and enhanced service features, such as text and video messaging and web browsing.



Strong customer growth, higher ARPC and an increase in average minutes of use led to wireless revenue growth of 13.8 per cent in 2005 compared to 2004.

Year over year, our customer base grew 11.9 per cent, with net activations of 75,830 up by 35.2 per cent over 2004, as we expanded our coverage area and digital wireless network, enhanced our dealer network and offered a broad product selection. At December 31, 2005, approximately 90 per cent of Atlantic Canada’s population had access to our digital wireless network, up from approximately 88 per cent at the same time last year. Our postpaid customer turnover rate, or churn, has improved over the prior year and remains industry-leading at 1.24 per cent, as a growing

number of our customers are subscribing to value packages, business bundles and longer-term contracts.

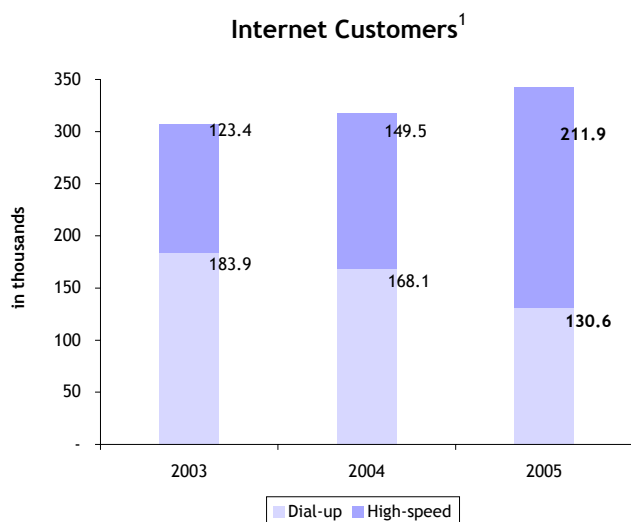
ARPC grew by 4.0 per cent in 2005. Postpaid ARPC increased by 4.7 per cent reflecting increased average minutes of use and significantly higher data usage, driven by text messaging, Web browsing, Blackberry® and premium content downloads. Prepaid ARPC increased by 24.3 per cent as new customers have generally had higher-usage than those disconnecting. Also, more customers are subscribing to value-added services offered in some of our prepaid plans.

Wireless - statistics

| <i>For the years ended December 31</i> | 2005 | 2004 | % change |
|---|-----------------|-------------|-----------------|
| Customers | 715,493 | 639,663 | 11.9 |
| Monthly - Average revenues per customer (dollars) | | | |
| Postpaid | \$ 57.99 | \$ 55.40 | 4.7 |
| Prepaid | \$ 13.44 | \$ 10.81 | 24.3 |
| Total | \$ 52.74 | \$ 50.71 | 4.0 |
| Gross activations | 181,506 | 160,511 | 13.1 |
| Deactivations | 105,676 | 104,428 | 1.2 |
| Net activations | 75,830 | 56,083 | 35.2 |
| Monthly - Average minutes of use per customer | 293 | 270 | 8.5 |
| Postpaid churn | 1.24% | 1.36% | (8.8) |

Internet revenue

Internet revenue is earned through high-speed and dial-up service to consumer and business markets and through enhanced services and applications, such as TV on my PC™, security services, music download service and dial-up accelerator.



¹ During the third quarter of 2005, we adjusted our dial-up customer base as it was determined to be overstated in the fourth quarter of 2004 by 7,099 customers.

Internet revenue grew by 10.7 per cent in 2005, driven by high-speed customer growth and increased adoption of enhanced services.

Our high-speed customer base grew 41.8 per cent over year-end 2004, contributing to total Internet customer growth of 7.9 per cent for the year ended December 31, 2005. Net customer additions for high-speed service were 139.6 per cent higher than in 2004, largely due to successful back to school and Christmas marketing programs, proactive management of dial migration, expansion of our service area, success in marketing our new small business Internet service, and customers adopting our popular PC purchase program. The reduction in our dial-up customer base continues to reflect migration to high-speed service, encouraged through

targeted promotions and our general introductory offers.

At December 31, 2005, our high-speed Internet service passed 81 per cent of homes and 85 per cent of businesses in Atlantic Canada, up from 72 per cent and 79 per cent, respectively, at the end of 2004. Our continued focus on customer retention and loyalty management programs mitigated the impact competition has on churn through our long-term customer contracts and the continued success of value packages and business bundles that integrate Internet offers with other products.

Internet - statistics

| <i>For the years ended December 31</i> | 2005 | 2004 | % change |
|---|-------------|-------------|-----------------|
| Operating revenue (millions of dollars) | | | |
| Dial-up | \$ 40.1 | \$ 45.3 | (11.6) |
| High-speed | \$ 91.8 | \$ 73.8 | 24.5 |
| Total | \$ 131.9 | \$ 119.1 | 10.7 |
| Monthly - Average revenue per customer (dollars) | | | |
| Consumer dial-up | \$ 20.02 | \$ 19.90 | 0.6 |
| Consumer high-speed | \$ 32.84 | \$ 33.14 | (0.9) |
| Business dial-up | \$ 47.35 | \$ 45.34 | 4.4 |
| Business high-speed | \$ 86.85 | \$ 98.95 | (12.2) |
| Net additions | | | |
| Dial-up | (37,510) | (15,793) | (137.5) |
| High-speed | 62,458 | 26,073 | 139.6 |
| Total | 24,948 | 10,280 | 142.7 |
| High-speed churn | | | |
| Consumer | 1.63% | 1.52% | 7.2 |
| Business | 1.80% | 2.15% | (16.3) |

As anticipated, business high-speed ARPC decreased in 2005 due to our strategic initiative to introduce new products targeted specifically at the small business customer. Our consumer high-speed ARPC decreased slightly in 2005 as the decline due to customers on short-term introductory offers during the first half of the year was mostly offset by the growing adoption of ultra high-speed service, security services and TV on my PC™ service in the second half of the year.

Other revenues

For the years ended December 31

(millions of dollars)

| | 2005 | 2004 | % change |
|---------------|----------|----------|----------|
| Product | \$ 124.4 | \$ 109.7 | 13.4 |
| Directory | 53.3 | 49.5 | 7.7 |
| Innovatia | 39.8 | 27.5 | 44.7 |
| Miscellaneous | 16.4 | 11.2 | 46.4 |
| | \$ 233.9 | \$ 197.9 | 18.2 |

The increase in product sales in 2005 reflects the impact of last year's work stoppage when limited resources caused product sales efforts to be significantly reduced, as well as revenues from our PC purchase program launched in mid-2005. Innovatia's revenue for 2005 increased when compared with the prior year due to new business, and miscellaneous revenues increased due to the acquisition of the DownEast retail chain late in 2004.

IT services revenue

IT services revenue is earned through systems integration, software engineering, infrastructure services and other IT consulting.

IT service revenue grew 2.2 per cent in 2005 over 2004. Excluding the \$14.8 million impact of 2004 business unit divestiture activity, underlying growth for the year was a solid 10.5 per cent. Approximately half of the underlying growth is attributed to the acquisition of the Atlantic-based operations of Fujitsu Consulting (Canada) Inc. in late 2004. The remainder of the growth results from new contracts in a number of key industry sectors combined with organic growth in consulting services.

Fulfillment revenue

Fulfillment revenue is earned through the sale of computer hardware, accessories and packaged software.

Fulfillment revenue grew 5.3 per cent in 2005 with growth being driven by strength in the general economy that has driven strong growth in business IT equipment spending.

Expenses

For the years ended December 31

(millions of dollars)

| | 2005 | 2004 | % change |
|-------------------------------|------------|------------|----------|
| Expenses | | | |
| Operating expenses | | | |
| Cost of operating revenues | \$ 284.9 | \$ 265.5 | 7.3 |
| Pension and OPEBs cost | 97.4 | 75.7 | 28.7 |
| Other operating expenses | 928.2 | 953.1 | (2.6) |
| | 1,310.5 | 1,294.3 | 1.3 |
| Depreciation and amortization | 391.3 | 397.3 | (1.5) |
| Restructuring charge | - | 72.3 | - |
| | \$ 1,701.8 | \$ 1,763.9 | (3.5) |

Cost of operating revenues

The cost of operating revenues increased by 7.3 per cent year over year. The increase is primarily driven by the cost of goods sold associated with the 13.4 per cent increase in telecommunications product sales and the 5.3 per cent increase in IT fulfillment revenue compared to the prior year. Partially offsetting this was a decrease in toll terminating and contribution expenses, which together declined 15.9 per cent due to a combination of lower rates and fewer minutes.

Pension and OPEBs cost

For the years ended December 31

(millions of dollars)

| | 2005 | 2004 | % change |
|--------------------------------|---------|---------|----------|
| Defined benefit | \$ 73.1 | \$ 48.5 | 50.7 |
| Defined contribution | 7.3 | 11.7 | (37.6) |
| Other post-employment benefits | 17.0 | 15.5 | 9.7 |
| | \$ 97.4 | \$ 75.7 | 28.7 |

DB pension cost for 2005 increased over 2004 primarily due to higher amortization costs arising from prior years' net actuarial losses and past service costs. The net actuarial losses have increased due to a rise in the accrued benefit obligation resulting from lower interest rates; the past service costs relate to plan amendments made in 2004. In addition, the plan amendments made in 2004 resulted in a higher current service cost for 2005 due to an increased number of active members in our DB plans. In 2005, we amortized \$15.6 million more accumulated losses and past service costs and incurred \$6.1 million more current service cost than in 2004.

Defined contribution (DC) pension cost represents the current service expense associated with our contributions to employees' retirement savings accounts. DC pension costs for 2005 were lower than for 2004 mainly due to fewer employee members in our DC pension plan, as certain eligible employees converted their membership from a DC plan to a DB plan pursuant to the 2004 plan amendments.

Other operating expenses

Overall, other operating expenses decreased by \$24.9 million, or 2.6 per cent, over 2004. This decline reflects approximately \$42 million of incremental one-time costs experienced during the 2004 work stoppage. Other general expense growth is being contained despite the cost pressure required to support growth in our wireless and Internet businesses through operating expense management and productivity improvements and cost savings generated by the 2004 ERIP, estimated to be \$39 million for the year.

Depreciation and amortization

Depreciation and amortization expense decreased due to lower capital investment being made in recent years, particularly during 2004 when capital programs were scaled back during the labour disruption. An acceleration of depreciation rates over the last few years has offset this decline as newer investments are increasingly being made in shorter-life assets.

Restructuring charge

During 2004, we incurred one-time costs to restructure our operations as we offered a voluntary ERIP to eligible employees, which resulted in a charge of \$66.6 million. There were no similar programs in 2005.

Other expenses

Other income (expenses)

Other income (expenses) includes non-operating items, such as interest income, gains on sale of assets, provincial large corporation tax and expenses related to our accounts receivable securitization program. For 2005, other income decreased mainly due to lower interest income from lower cash balances and higher foreign currency losses when compared with 2004.

Interest charges

Interest charges for 2005 were slightly lower than the prior year. Although our average long-term debt balance throughout 2005 was higher when compared with 2004, a lower interest rate on debt issued in May 2005, along with the benefit of swapping some of our fixed-rate interest payments for floating, has resulted in a lower interest expense for 2005.

Income taxes

Income taxes increased in 2005 by 74.6 per cent over 2004 mainly due to higher net income. Also contributing to the year-over-year increase was a reduction in income taxes in 2004 of \$9.5 million resulting from the reversal of a previously recorded tax liability following the favourable resolution of outstanding tax audits related to previous years.

Comparing 2005 to the prior year, the future tax expense component of income taxes has increased by \$14.7 million. This represents a shift from current tax expense to future tax expense, which occurs when there are higher deductions or lower additions to income calculated for tax purposes compared to reported income before tax. The increase in future tax expense for 2005 is a result of higher ERIP and pension related deductions offset by lower capital investment related deductions taken for tax purposes in 2005 than in 2004. In addition,

the reduction to income taxes in 2004 that resulted from the resolution of prior year tax issues was a reduction to the future tax expense component of 2004 income taxes.

Financial and capital management

Summary of cash flows

For the years ended December 31

(millions of dollars)

| | 2005 | 2004 | % change |
|---|-------------------|------------------|--------------|
| Cash from (used in): | | | |
| Operating activities | | | |
| Net income | \$ 199.4 | \$ 130.7 | 52.6 |
| Adjustments to reconcile net income to cash from operating activities | | | |
| Net benefit plans cost | 90.1 | 64.0 | 40.8 |
| Funding of DB pension and OPEBs plans | (172.6) | (87.1) | 98.2 |
| Change in non-cash working capital | 5.9 | 76.5 | (92.3) |
| Depreciation, amortization and other non-cash items | 401.5 | 391.7 | 2.5 |
| | 524.3 | 575.8 | (8.9) |
| Repurchase of common shares | \$ (161.4) | \$ (50.6) | 219.0 |
| Cash dividends paid on preferred and common shares | (121.2) | (150.4) | (19.4) |
| Proceeds of long-term debt | 149.1 | - | - |
| Repayment of long-term debt | (151.4) | (100.1) | 51.2 |
| Purchase of capital investments | (363.2) | (293.4) | 23.8 |
| Business acquisitions, net of cash | (0.6) | (23.4) | (97.4) |
| Other financing and investing activities | (3.9) | - | - |
| Net decrease in cash | \$ (128.3) | \$ (42.1) | 204.8 |

Operating activities

During 2005, we generated \$524.3 million in cash from operating activities, a decrease of \$51.5 million over 2004. Higher net income for the year was offset by higher pension plan contributions and a decline in cash generated from changes in working capital.

Net benefit plans cost

Included in net benefit plans cost are DB pension and OPEBs costs. These are added back to net income to arrive at cash from operating activities as they are non-cash costs replaced by the actual cash funding requirements discussed below. Refer to the "Pension and OPEBs cost" section for a discussion of these items.

Funding of DB pension and OPEBs plans

The amounts we contributed to our pension plans in 2005 significantly exceeded our 2004 funding contributions. The increase reflects voluntary contributions made in February 2005 as well as additional required funding resulting from actuarial valuations that were performed effective December 31, 2004, and completed in late 2005. The required DB pension plan funding for 2005 was \$120.0 million, which is considerably higher than the \$70 million to \$80 million that we estimated for the year. It is very difficult to accurately project pension funding requirements due to the impact that changes in assumptions can have on the pension assets and liabilities and the complexity of the actuarial calculations. Refer to the “Risk and risk management” section discussion on “Pension and OPEB contributions”.

Change in non-cash working capital

For the years ended December 31

(millions of dollars)

| | 2005 | 2004 | % change |
|-------------------------------------|----------|---------|----------|
| Accounts receivable | \$ (8.3) | \$ 41.3 | - |
| Prepayments | (2.8) | 5.6 | - |
| Inventory | (7.5) | 0.7 | - |
| Payables and accruals | (71.4) | 42.4 | - |
| Income taxes receivable and payable | 95.9 | (13.5) | - |
| Change in non-cash working capital | \$ 5.9 | \$ 76.5 | (92.3) |

In 2005, we generated \$5.9 million from changes in non-cash working capital, a significant decrease from 2004. In 2004, there was a significant decrease in accounts receivable due to strong collection of customer accounts and to the divestiture of business units. The accounts receivable balance has increased slightly in 2005 over 2004, reflecting operating revenue growth. The lower payables and accruals balance at the end of 2005 is mainly due to payments to retirees related to our ERIP, reducing the \$66.6 million accrual recorded in December 2004. Inventory increased in 2005 to supply aggressive holiday promotions. These and other small decreases in cash from working capital changes were offset by the receipt of an income tax refund of approximately \$55 million and lower income tax installments.

Depreciation, amortization and other non-cash items

Depreciation and amortization expense decreased by \$6.1 million in 2005. Refer to the “Depreciation and amortization” section for a discussion of this item.

Repurchase of common shares

Under the NCIB that commenced on August 6, 2003, and ended August 5, 2004, we acquired our common shares for cash at the market price through the facilities of the TSX. We commenced a similar but new NCIB on February 4, 2005, under which we may acquire an additional 6,637,200 common shares prior to the expiry of the bid on February 3, 2006.

For the year ended December 31, 2005, we purchased for cancellation 5,797,715 shares (2004 - 1,732,130 shares) for an aggregate price of \$161.4 million (2004 - \$50.6 million).

Further details about the NCIB are provided in note 13 to our consolidated financial statements for the year ended December 31, 2005. Shareholders may obtain a copy of the Notice of Intention that was filed with the TSX in relation to the NCIB by contacting us at investor.relations@aliant.ca.

Cash dividends paid on preferred and common shares

Common share dividends declared in 2005 increased by 4.7 per cent. There was a 7.3 per cent increase in the annual common share dividend to \$1.18 for 2005. This was partially offset by fewer shares outstanding as a result of the NCIB. However, cash dividends paid during 2005 declined as the fourth quarter payment that would normally have been paid on December 30, 2005, was deferred until January 3, 2006, to allow shareholders to benefit from dividend tax savings announced by the federal government.

We also paid preferred share dividends of \$9.5 million in 2005 (2004 - \$9.5 million).

Proceeds and repayments of long-term debt

In May 2005, we issued \$150.0 million (for net proceeds received of \$149.1 million) in seven-year notes, pursuant to a shelf prospectus filed on May 9, 2005. The notes bear interest of 4.52 per cent per annum, mature on May 24, 2012, and are callable at any time at the greater of par and the Canada Yield Price. The proceeds of this issue were used to repay \$150.0 million in medium-term notes that matured in November 2005.

Purchase of capital investments

Capital investments made in 2005 outpaced 2004 by a significant margin as 2004 spending was hampered by the work stoppage and 2005 saw us aggressively advance our strategy of growth and transformation. We have continued to invest in our traditional wireline as required and have increased our investment in wireless and Internet. During 2005, we expanded and augmented our high-speed Internet footprint, began the transformation of our network to support next-generation IP applications and launched Aliant TV. Increased levels of investment were also directed toward transforming our cost structure, improving our customer experience, and sustaining our existing business and reliability.

Business acquisitions, net of cash

During 2004, we purchased DownEast and the Atlantic Canada operations of Fujitsu Consulting (Canada) Inc. for combined cash consideration of \$23.4 million. In 2005, a small amount of costs were incurred to finalize the purchases.

Other financing and investing activities

We paid \$5.0 million in each of 2005 and 2004 to repurchase a portion of the accounts receivable sold under a securitization program. The accounts receivable securitization program is discussed further in the “Off-balance sheet arrangements” section.

We also acquired \$12.0 million worth of capital equipment through capital lease transactions during 2005, the details of which are discussed in note 11 to our consolidated financial statements for the year ended December 31, 2005.

Liquidity

Cash requirements

Our cash requirements for 2006 will consist of investments in capital, dividend payments, required pension plan contributions and payments of other commitments. In particular these requirements will result in the use of cash as follows:

- Capital investments will be made as required to support our existing infrastructure and to advance our strategies of growth and transformation.
- Common share dividends of \$37.6 million relating to the fourth quarter of 2005 were paid on January 3, 2006. Common dividends at a rate of \$0.31 per share per quarter, commencing with the March 2006 dividend, and preferred share dividends will be paid, totalling approximately \$42 million per quarter, or \$168 million annually. To the extent that shares may be repurchased under an NCIB or preferred shares are redeemed, the total cash required for dividend payments will be slightly reduced.
- Total funding of our pension and OPEB plans for 2006 is anticipated to be in the range of \$120 million to \$130 million. We are contributing monthly to our pension plans based on this estimate and we do not plan to make any additional voluntary contributions in 2006. DB pension plan actuarial valuations for the year ended December 31, 2005, will be completed in the first half of 2006 and we will adjust our DB pension plan contributions if necessary based on the outcome of these valuations. Further details of our pension contribution requirements are discussed in the “Other financial arrangements” and “Risk and risk management” sections.
- Our accounts receivable securitization program expires in December 2006. Should we decide not to renew the program, we would be required to repurchase \$120.0 million of our accounts receivable.
- We have long-term debt totalling \$90.0 million that is callable in March and July of 2006. Given current interest rates, it is our expectation that this debt will be called at the first available dates.
- Other commitments, such as operating leases and purchase commitments for equipment and other network infrastructure, and contingencies as disclosed in notes 19 and 22 to our consolidated financial statements for the year ended December 31, 2005.

Sources of liquidity

We anticipate that we will be able to meet our future cash requirements from cash on hand, the generation of cash from operating activities, and through access to the capital markets and credit facilities as described below.

Capital structure

As at December 31

(millions of dollars, except as otherwise noted)

| | 2005 | | 2004 | | | |
|--|------|---------|--------|----|---------|--------|
| Common equity | \$ | 1,239.6 | 53.1% | \$ | 1,358.4 | 55.6% |
| Preferred equity | | 172.3 | 7.4% | | 172.3 | 7.1% |
| Non-controlling interest | | 5.6 | 0.2% | | 5.2 | 0.2% |
| Long-term debt, including amount due within one year | | 904.5 | 38.8% | | 896.4 | 36.7% |
| Notes payable and bank advances | | 11.2 | 0.5% | | 9.1 | 0.4% |
| Total capital | \$ | 2,333.2 | 100.0% | \$ | 2,441.4 | 100.0% |
| Debt as a percentage of total capital | | | 39.3% | | | 37.1% |

Common equity

At January 20, 2006, we had the following outstanding shares and stock options:

Authorized

Unlimited number of preference shares, issuable in series.

Unlimited number of common shares, without par value.

Issued

As at January 20, 2006

(millions of dollars, except as otherwise noted)

| | Number of shares | Value |
|-----------------------------|------------------|------------|
| Preference shares, Series 2 | 7,000,000 | \$ 172.3 |
| Common shares | 127,193,610 | 1,005.3 |
| | | \$ 1,177.6 |

| | Number of options | Weighted average exercise price |
|---------------------|-------------------|---------------------------------|
| Options outstanding | 2,884,809 | \$ 30.31 |
| Options exercisable | 2,076,797 | \$ 30.42 |

Preferred equity

Our preferred shares are redeemable for par value of \$175.0 million at our option on June 30, 2006. Alternatively these can remain outstanding with a re-set dividend rate. It is our intention that the dividend rate will be re-set on June 30, 2006, and every 5 years after that date, and that these will remain a permanent component of our capital structure.

Debt

We maintain excellent access to capital markets, which provides flexibility in our capital structure. We filed a shelf prospectus in May 2005 that allows us to issue up to \$350.0 million in medium-term notes as and when we require funds during its 25-month life. As noted above, we issued \$150.0 million in medium-term notes in the second quarter of 2005. A further \$200.0 million is permitted under the shelf prospectus.

As at December 31, 2005, we maintained committed and other operating lines of credit totalling \$686.0 million, an increase of \$49.5 million over 2004, which was required to support specific letters of credit. There was \$10.5 million drawn on our operating lines of credit and \$19.8 million of letters of credit were committed against our operating lines of credit at the end of 2005. Further details on our existing credit arrangements are provided in note 9 to our audited consolidated financial statements for the year ended December 31, 2005.

Credit ratings

During the second quarter of 2005, Standard and Poors (S&P) and Dominion Bond Rating Service (DBRS) adjusted the outlook, or trend, on our corporate credit ratings from stable to negative, except for the rating of Aliant's commercial paper program, which remained stable.

Then, during the fourth quarter of 2005, DBRS downgraded our corporate credit and long-term debt ratings, but resumed a stable trend for the rating. Again, the short-term rating on Aliant's commercial paper program remained unchanged. Our ratings at December 31, 2005, and comparative ratings at December 31, 2004, were as follows:

| | Rating at December 31, 2005 | | Rating at December 31, 2004 | |
|---|-----------------------------|---------------------------|-----------------------------|--------------------------|
| | S&P | DBRS | S&P | DBRS |
| Aliant corporate credit rating | A negative outlook | BBB (high) stable trend | A stable outlook | A (low) stable trend |
| Aliant preferred shares | P-2 (high) | Pfd-3 (high) stable trend | P-2 (high) | Pfd-2 (low) stable trend |
| Aliant commercial paper | A-1 | R-1 (low) stable trend | A-1 | R-1 (low) stable trend |
| Aliant Telecom unsecured long-term debt | A | A (low) stable trend | A | A stable trend |

The adjustments generally reflect the expectation by these rating agencies of increased competition in local services as cable companies launch VoIP services in Canada.

Other financial arrangements

Off-balance sheet arrangements

Contractual obligations

We have various operating leases and purchase commitments for equipment and other network infrastructure. The amounts of estimated future payments under such arrangements are detailed as follows.

As at December 31, 2005

| (millions of dollars) | 2006 | 2007 | 2008 | 2009 | 2010 | Thereafter |
|--|---------|----------|---------|----------|---------|------------|
| Long-term debt | \$ 1.3 | \$ 101.3 | \$ 1.4 | \$ 105.0 | \$ 46.5 | \$ 635.0 |
| Capital lease obligations | 5.4 | 3.3 | 2.5 | 1.5 | 1.3 | - |
| Operating leases | 43.2 | 38.5 | 36.3 | 34.5 | 28.5 | 120.4 |
| Purchase commitments ¹ | 39.2 | 9.4 | 3.9 | 1.9 | - | - |
| Total contractual obligations ² | \$ 89.1 | \$ 152.5 | \$ 44.1 | \$ 142.9 | \$ 76.3 | \$ 755.4 |

¹ Purchase commitments are agreements to purchase goods or services that are enforceable and legally binding on us and specify all significant terms, including: fixed or minimum quantities to be purchased; fixed minimum or variable price provisions; and the approximate timing of the transaction.

² We have other long-term liabilities that are not included in the table. They consist of an accrued benefit liability, a future income tax liability, deferred revenue, and various other long-term liabilities.

Accounts receivable securitization

We participate in a program whereby we can sell up to \$125.0 million of certain accounts receivable to a securitization trust. At December 31, 2005, net cash proceeds in our securitization trust totalled \$120.0 million, reflecting \$5.0 million of our accounts receivable that were repurchased during the year. The security required under the program, recorded as retained interest, was \$39.5 million at December 31, 2005. The terms of the purchase and sale arrangement and accounting policy that we follow are described in notes 1 and 2 to our consolidated financial statements for the year ended December 31, 2005.

Use of derivative financial instruments

We use derivative financial instruments periodically in the management of interest rate or foreign currency exposures associated with our long-term debt or specific firm commitments. Details of our use of derivative financial instruments and accounting policies we follow are provided in notes 1 and 18 to our consolidated financial statements for the year ended December 31, 2005. The following derivative financial instruments were outstanding at December 31, 2005:

- An interest rate swap transaction with a notional amount of \$100.0 million expiring in May 2011. This swap was entered into in order to adjust the mix of floating and fixed rate debt utilized within our targeted capital structure. This swap results in us exchanging our underlying fixed interest rate of 6.80 per cent per annum for a three-month Banker's Acceptance floating interest rate plus 2.06 per cent. The terms of the swap transaction are unchanged from December 31, 2004.

- Interest rate swaption transactions relating to two outstanding issues of long-term debt with a total notional amount of \$90.0 million. These swaptions grant an option to the counterparty in the transaction to enter into an interest rate swap transaction with us on the call dates of the two underlying debt instruments. As a result of entering into these agreements, we received premium income payments from the counterparty of \$7.6 million in 2001 and \$5.4 million in 1997. This premium income is being amortized against interest charges over the period to maturity of the underlying debt issues. The remaining unamortized premium income at December 31, 2005, of \$7.4 million is recorded as a deferred credit. The terms of the swaption are unchanged from December 31, 2004.

Given current and forecasted interest rate levels over the next year, we anticipate the financial institution counterparty will exercise the two interest rate swaption agreements upon their expiry dates in March and July of 2006. The exercise of these swaptions will cause us to be placed into a fixed-floating interest rate swap until maturity in 2013. We will pay fixed interest payments of 10.45 per cent on a notional principal of \$50.0 million and 11.125 per cent on a notional principal of \$40.0 million and, in return, we will receive floating interest payments related to the three-month Banker's Acceptance rates. At December 31, 2005, the fair value of these agreements is \$34.4 million in favour of the counterparty. The fair value, less unamortized premium income of \$7.4 million results in a \$27.0 million deferred loss that is not recorded in our financial statements due to the application of hedge accounting treatment to these transactions. If the agreements were to be cancelled and the \$90.0 million of underlying long-term debt repaid as of December 31, 2005, this amount would have to be recorded as a loss on our income statement. Given current interest rates, it is our expectation that the swaptions will be exercised by the counterparty and the long-term debt will be called by us in 2006. The actual loss that will be recorded on the swaptions will depend on interest rate levels in effect on the exercise dates in 2006.

Pension plan obligations and related cash requirements

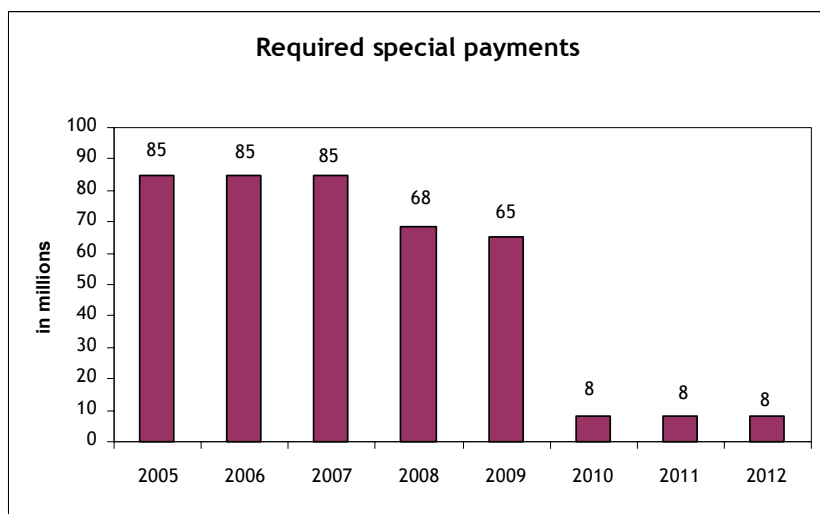
We provide certain pension plans to qualified employees. These include DC pension plans, DB pension plans and retirement savings plans. Details of our post-employment benefits and the accounting policies we follow are provided in notes 1 and 6 to our consolidated financial statements for the year ended December 31, 2005.

Our DB pension plans require periodic funding payments to a trust fund, which are determined by performing required actuarial valuations of the plans. During 2005, we completed the actuarial valuations of our DB pension plans as of December 31, 2004. These valuations prescribed our required funding obligation for 2005 to be \$120.0 million. We contributed \$167.3 million during 2005, which included our prescribed funding and \$60.0 million in voluntary contributions. During the fourth quarter of 2005, \$17.3 million of our voluntary contributions were reallocated against required funding and we expect the remainder will be utilized to reduce required funding over the next two to three years.

In late 2004, we amended our DB pension plans to include enhancements to certain features and to increase past service benefits accrued for some employees. In addition, we offered an ERIP, which was accepted by approximately 650 DB plan members. The actuarial valuations performed as of December 31, 2004, reflect the increased liability resulting from these plan

changes and also reflect the impact of declining actuarial discount rates. Although much of the impact of the aforementioned factors was anticipated, the actual impact on the solvency position of the plans was greater than we anticipated. As of December 31, 2004, each of our four DB pension plans experienced a solvency deficiency position. Regulations prescribe that solvency deficiencies must be funded with special payments over five years. As such, our required special payments for 2005 were approximately \$40 million higher than we anticipated.

Based on the funded position of our DB pension plans as of December 31, 2004, our special payments required over the next eight years (including 2005) are shown below. Special payments are payments above any current service contributions and are specifically required to eliminate funding deficits.



Federal pension regulation also requires that plans with solvency deficiencies file annual valuations. Therefore, actuarial valuations will be required for all of our DB pension plans as of December 31, 2005, and will be performed during the first half of 2006. Given changes in interest rates and the unpredictability of equity market returns, our pension plans' funded status is constantly changing. The annual valuation requirement will lead to volatility in our funding requirements. The option to utilize

voluntary contributions previously made against future required funding will help us to mitigate some of this volatility.

OPEB plans

We provide OPEBs to qualifying retirees, including life insurance, health and dental plans. Details of our post-employment benefits and the accounting policies we follow are provided in notes 1 and 6 to our consolidated financial statements for the year ended December 31, 2005.

In January 2006, we announced significant changes to the OPEB plans we will be providing our future retirees. The legacy plans will continue to exist for current retirees and certain eligible employees that are close to retirement. All remaining employees will now participate in an OPEB plan whereby an annual benefit is capped at a defined dollar amount that the employee may use to purchase benefits, through group arrangements, annually upon retirement. Employees hired after January 15, 2006, will be able to access group plan rates when they retire, but will not receive any contribution toward these costs from Aliant.

We expect the new program to significantly reduce the amount and the volatility of our OPEB costs in the future.

Related party transactions

Bell Canada, which is owned 100 per cent by BCE Inc., beneficially owns and controls 53.21 per cent of our outstanding common shares as at December 31, 2005. In the normal course of business, we engage in transactions with our majority shareholder and its controlled investees to purchase and provide telecommunications and other support services and to purchase capital investments. In addition, during the year, we repurchased common shares from Bell Canada under our NCIB program. At December 31, 2004, we had notes receivable with Bell Canada, which were repaid and reissued on a revolving demand basis throughout the year. All of these notes were repaid as of December 31, 2005. Refer to note 20 of our consolidated financial statements for the year ended December 31, 2005, for greater detail on our related party transactions.

Significant accounting policies

Our consolidated financial statements have been prepared in accordance with Canadian GAAP. Greater detail on our significant accounting policies is provided in note 1 to our consolidated financial statements for the year ended December 31, 2005. The accounting policies and methods used are consistent with those in effect in 2004, except as otherwise noted.

Accounting policy changes in 2005

Effective January 1, 2005, we changed our accounting policies for subscriber acquisition costs and the recognition of our directory revenue and expenses, to provide more relevant presentation of these items in the financial statements. Further details on these changes in accounting policies are presented in note 1 of our consolidated financial statements for the year ended December 31, 2005.

Future changes in accounting policies

The Accounting Standards Board (AcSB) of the Canadian Institute of Chartered Accountants (CICA) continually amends and improves certain standards or guidelines contained in the CICA Handbook. We monitor these changes as they are proposed and will make changes to our accounting policies and disclosures as necessary.

Non-Monetary Transactions

In June 2005, the AcSB issued a new Section 3831, Non-Monetary Transactions, replacing Section 3830 of the same title. It requires all non-monetary transactions to be measured at fair value unless certain specific criteria apply. The new requirements are effective for non-monetary transactions initiated in periods beginning on or after January 1, 2006, and are not to be applied retroactively.

Comprehensive Income

The CICA issued section 1530 of the CICA Handbook, Comprehensive Income. The section is effective for fiscal years beginning on or after October 1, 2006. It describes how to report and disclose comprehensive income and its components. Comprehensive income is the change in a company's net assets that results from transactions, events and circumstances from sources

other than the company's shareholders. It includes items that would not normally be included in net earnings, such as unrealized gains or losses on available-for-sale investments.

The CICA also made changes to section 3250 of the CICA Handbook, Surplus, and reissued it as section 3251, Equity. The section is also effective for fiscal years beginning on or after October 1, 2006. The changes in how to report and disclose equity and changes in equity are consistent with the new requirements of section 1530, Comprehensive Income.

Adopting these sections on January 1, 2007, will require us to start reporting the following items in the consolidated financial statements:

- Comprehensive income and its components; and
- Accumulated other comprehensive income and its components.

Financial Instruments - Recognition and Measurement

The CICA issued section 3855 of the CICA Handbook, Financial Instruments - Recognition and Measurement. The section is effective for fiscal years beginning on or after October 1, 2006. It describes the standards for recognizing and measuring financial assets, financial liabilities and non-financial derivatives. This section requires that:

- All financial assets be measured at fair value, with some exceptions, such as loans and investments that are classified as held-to-maturity;
- All financial liabilities be measured at fair value if they are derivatives or classified as held for trading purposes. Other financial liabilities are measured at their carrying value; and
- All derivative financial instruments be measured at fair value, even when they are part of a hedging relationship.

We are currently evaluating the impact on our consolidated financial statements of adopting this section on January 1, 2007.

Hedges

The CICA recently issued section 3865 of the CICA Handbook, Hedges. The section is effective for fiscal years beginning on or after October 1, 2006, and describes when and how hedge accounting can be used. Hedging is an activity used by a company to change an exposure to one or more risks by creating an offset between:

- Changes in the fair value of a hedged item and a hedging item;
- Changes in the cash flows attributable to a hedged item and a hedging item; or
- Changes resulting from a risk exposure relating to a hedged item and a hedging item.

Hedge accounting ensures that all gains, losses, revenues and expenses from the derivative and the item it hedges are recorded in the income statement in the same period. We are currently evaluating the impact on our consolidated financial statements of adopting this section on January 1, 2007.

Critical accounting estimates and assumptions

Under Canadian GAAP, we are required to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosures of contingent assets and liabilities in the financial statements.

We base our estimates and assumptions on past experience and other factors that we believe are reasonable under the circumstances. This involves varying degrees of judgment about matters that may be inherently uncertain. The amounts currently reported in the financial statements could prove to be inaccurate or are subject to change under different conditions or using different assumptions. We periodically evaluate the reasonability of these estimates and assumptions.

Our senior management have reviewed with the audit committee of the board of directors the development, selection and application of our key accounting policies and the critical accounting estimates and assumptions they involve. We consider the critical accounting estimates and assumptions described in this section to be an important part in understanding our significant accounting policies and consolidated financial statements.

Post-employment benefits

We perform a valuation of our DB pension plans at least every three years to determine the actuarial present value of the accrued pension and other non-pension post-employment benefits. The amounts reported in the financial statements in relation to the DB pension plans and OPEB plans are determined using the results of these valuations and several key assumptions determined by management. These key assumptions include the rate used to discount obligations, the expected rate of return on plan assets, the rate of compensation increase and the growth rate of per capita health care costs.

Our two most significant assumptions are the discount rate and the rate of return on plan assets. Our telecommunications segment is affected by these assumptions. The rates are developed as follows:

- The discount rate is used to determine the present value of future cash flows that we expect will be required to pay employee benefit obligations. Management's assumptions of the discount rate are based on current interest rates on long-term debt of high quality corporate issuers. We determine the appropriate discount rate at the end of every year. Given the continued decline in long-term bond yields during 2005, we have lowered our assumed discount rate from 6.25 per cent to 5.25 per cent, effective December 31, 2005. This change in assumption increased our DB pension plan and OPEB plan obligations by \$281.4 million and \$31.7 million, respectively, at the end of 2005. These amounts are included as actuarial losses in the "Components of accrued benefit asset (liability)" table in note 6 to our consolidated financial statements for the year ended December 31, 2005.
- The expected rate of return on plan assets is based on the long-term return expectation for capital markets and active investment management, given our plans' policy asset mix. We review the expected rate of return at the end of every year and have determined our assumption for 2005 to be consistent with 2004.

A sensitivity table outlining the estimated impact on the value of the accrued benefit obligation and the annual amount of net benefit plans' cost for a 0.25 percentage point change in these rate assumptions is provided in note 6 to our consolidated financial statements for the year ended December 31, 2005.

Our accounting policies with respect to the recognition of amortization on net actuarial losses follow Canadian GAAP and recognize that future investment returns on plan assets and actuarial changes in the plans can influence the amount of the loss and can reverse it over time. Specifically, the amortization occurs when the size of the actuarial loss (or gain) exceeds a 'corridor', which is the greater of 10 per cent of the accrued benefit obligation or 10 per cent of the market-related value of the plan assets. Using the market-related value of assets smoothes the affect of actual gains and losses in the plans' equity assets over a three-year period. The effect of these accounting policies is to limit the amount of amortization of both gains and losses recognized in our earnings, except in situations when they become exceedingly large. We have unamortized actuarial losses totalling \$707.3 million in our DB pension plans at the end of 2005. This balance reflects the amortization of \$29.5 million of the losses through pension expense in 2005. In 2006, we estimate that our pension expense will include loss amortization in the range of \$35 million to \$36 million. The impact of prior year unamortized actuarial losses on future pension expense cannot be determined with certainty because it will be influenced by experience in future years.

Additional information regarding our accounting for post-employment benefits is included in note 6 to our consolidated financial statements for the year ended December 31, 2005.

Long-lived assets

Our long-lived assets consist of capital investments, goodwill and indefinite-life intangibles. We make certain estimates relating to the values recorded for these assets, including determinations of useful life, assessments of asset recoverability through impairment testing and the allocation of acquisition purchase prices between goodwill and finite-life intangible assets.

Estimations of useful lives

We depreciate and amortize our capital investments, finite-life intangibles and certain deferred charges based on their estimated useful lives. We estimate the useful life when an asset is acquired, based on past experience with similar assets and our expectations of technological changes or other circumstances that may affect the usefulness of the asset. We review our estimates of useful life on an ongoing basis. When events or changes in circumstances indicate that asset lives do not reflect the expected remaining period of benefit, we make prospective changes to their depreciable useful lives. This could result in a change in the depreciation and amortization expense in future periods.

Recoverability

The value associated with our goodwill is assessed at our operating segment level on an annual basis or sooner if events or changes in circumstances indicate that the carrying amounts could exceed fair value. Potential impairment is identified when the carrying value of our business segments, including the allocated goodwill, exceeds their fair value. Goodwill impairment is measured as the excess of the carrying amount of the business segment's allocated goodwill

over the implied fair value of the goodwill, based on the fair value of the assets and liabilities of the business segment. Any impairment indicated is charged to earnings in the period such impairment is identified. The annual impairment test that we conducted during the second quarters of 2005 and 2004 indicated that no impairment provision was required. There have been no events or circumstances since that time indicating impairment.

The value associated with our indefinite-life intangibles is assessed on an annual basis or sooner if events or changes in circumstances indicate that the carrying amounts could exceed fair value. The value associated with our other long-lived assets is reviewed whenever events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable. Recoverability is based on our estimate of projected discounted cash flows resulting from the use of the asset and its eventual disposition. These reviews could result in a current year impairment charge to reflect the writedown in value of the capital investment or long-lived asset. Reviews triggered by events or changes in circumstances throughout 2005 and 2004 have not resulted in any writedowns for impairment of our other long-lived assets.

We use the projected discounted cash flow method to measure fair value and determine recoverability of assets, which we believe is a reasonable and appropriate approach to measure fair values. The assumptions and estimated cash flows are based on internal planning and reflect our best estimates. These assumptions are subject to inherent uncertainties that are beyond management's control; hence the results of the impairment test could be different if there is a change in assumptions or conditions. We are unable to predict whether an event that triggers impairment will occur, when it will occur or how it will affect the asset values that have been reported.

Purchase price allocation for a business acquisition

Goodwill represents the excess, at the date of acquisition, of the costs of an acquired business over the fair values of the net amounts assigned to the individual assets acquired and liabilities assumed, regardless of whether or not these items were recognized in the financial statements of the acquired business. Intangible assets other than goodwill are recognized at their estimated or appraised values when they arise from contractual or other legal rights or are capable of being individually sold, transferred, licensed, rented or exchanged. The identification and valuation of intangible assets of an acquired business involves the evaluation of all significant terms of the purchase that explicitly or implicitly suggest the presence of intangible assets apart from goodwill.

There were no changes in 2005 to the purchase price allocation for the businesses acquired in 2004 by our telecommunications and information technology segments. As well, there were no business acquisitions in 2005.

Income taxes

We use the asset and liability method to account for income taxes, which requires us to estimate the expected future tax consequences of temporary differences between the carrying amounts of assets or liabilities for financial reporting purposes compared with the tax basis of assets and liabilities and tax losses carried forward for tax purposes. The future tax consequences of the temporary differences, which impact the classification and calculation of our tax assets and liabilities, are based on assumptions and estimates related to expectations of

future results of operations, the timing of the reversal of temporary differences and our interpretation of applicable income tax legislation and regulations. The composition of our future income tax assets and liabilities are likely to change from period to period because of the significance of these assumptions.

The calculation of our income taxes also requires significant judgment and interpretation of tax regulations and legislation, which are continually changing, to ensure liabilities are complete and to ensure assets, net of valuation allowances, are realizable. As our tax filings are subject to audit by the Canada Revenue Agency (CRA), such audits could materially change the amount of current and future income tax assets and liabilities if different interpretations are used. The CRA is in the process of auditing Aliant Telecom Inc.'s 2000, 2001 and 2002 taxation years, with any findings expected to be reported to us in 2006.

We use judgments and estimates when calculating income taxes. If these prove to be inaccurate, or if certain tax rates or laws change, our results of operations and financial position could be materially impacted in future periods. We believe that we have adequately provided for income taxes based on all information currently available.

During 2005, we revised our estimate for the timing of certain temporary differences. There were no other significant changes to estimates during 2004 or 2005.

Restructuring charges

As circumstances require, we engage in restructuring activities to streamline our operations and improve productivity and profitability. The development of formal plans to execute these activities requires us to estimate costs related to post-employment benefits, severance and other employee related benefits, premise rationalization, technology lease cancellation penalties and other exit costs. We make these estimates based on the terms of any contracts involved, the number of employees, their pension eligibility and other related factors. Restructuring is a complex process that can take several months or longer to complete, requiring a periodic reassessment of original estimates. In addition, we constantly evaluate whether the estimates of the remaining liabilities under our restructuring program are appropriate. As a result, we may have to change previously reported estimates when the payments are made or activities completed. There may also be additional charges for new restructuring initiatives.

There were no changes in 2005 to the estimates or assumptions used to develop the 2004 restructuring charges liability. There were no new restructuring charges in 2005.

Legal and regulatory contingencies

We may become involved in various litigation and regulatory proceedings in the normal course of our business. Pending litigation, regulatory initiatives or regulatory proceedings represent potential financial loss. We accrue potential losses if we believe the loss is probable and can be reasonably estimated. Estimates of loss are based on consultation with legal counsel and involve analyzing potential outcomes and assuming various litigation and settlement strategies. Note 22 to our consolidated financial statements for the year ended December 31, 2005, presents a discussion of significant contingencies outstanding at that date.

None of our operating segments had any significant provisions relating to pending litigation or regulatory initiatives and proceedings at December 31, 2005. We have not made any significant changes to our estimates in the past two years.

Risk and risk management

Management is confident about our long-term prospects, but we recognize that we are exposed to a number of risks in the normal course of business that could have a negative effect on our financial condition or results of operations. The risks noted may not be exhaustive as there may be other risks that we are currently unaware of or that we presently consider insignificant to our consolidated operations.

Our corporate structure

Aliant Inc., as a corporate entity does not carry on any significant operations and has no major sources of income or assets, other than interest in its subsidiaries and a joint venture. Our financial performance and our ability to service our debt and pay dividends to our shareholders are dependent on the dividends and other distributions we receive from our interest in our subsidiaries and joint venture.

Our dependence on the telecommunications segment

Our financial performance is dependent on the performance of our subsidiaries and joint venture, in particular the performance of those interests that constitute our telecommunications segment. Therefore the risks that impact this segment are more likely to have a significant impact on the financial condition, results of operations and business of our company as a whole.

Stock market volatility

Stock markets are generally subject to significant volatility due to such factors as fluctuating interest rates, economic conditions and political uncertainty. This market volatility influences the market price and trading volumes of the shares of many companies. In particular, the shares of telecommunications companies have been experiencing price volatility due to industry factors such as competition, mergers and acquisitions activity, the debate over the merit of conversion to an income trust structure and regulatory developments. Differences between our actual or anticipated financial results and the published expectations of financial analysts may also contribute to volatility in our common shares. A major decline in the capital markets in general, or an adjustment in the market price or trading volumes of our common shares or other securities, may materially and negatively impact our ability to raise capital, issue debt, retain employees or make future strategic acquisitions or joint ventures.

Ability to achieve strategies and plans

We plan to achieve our business objectives in 2006 through the performance of key strategic initiatives under our continued strategy of growth and transformation. These initiatives are discussed under the “2006 strategic direction” section.

These initiatives will have a wide-reaching impact, transforming our customer interactions, our internal processes, our network and our people. If we are unable to attain these initiatives on a

timely basis or achieve the desired effect, we may be unable to meet our business objectives. As a result, our financial performance, including our growth prospects, could be negatively affected.

General economic conditions

Changes in general economic conditions, customer confidence and spending affect the demand for, and prices of, our products and services. In particular, a downturn in general economic conditions could lead to:

- Lower than anticipated demand for IT services and products and integrated ICT solutions;
- Lower than expected growth in data revenue due to softer demand from enterprise and wholesale customers;
- Lower than anticipated long distance and wireless revenues due to decreased usage; and
- Higher than anticipated bad debt expense due to increased credit risk.

The existence of these conditions or the emergence of new conditions could reduce revenues or increase costs, negatively affecting results. We constantly monitor economic conditions to enable us to respond by implementing strategies to mitigate risks or adjusting assumptions used in recording the effects of these risks on our results.

Pension plan funding

Our required DB pension and OPEB plan funding for 2006 is estimated to be in the range of \$120 million to \$130 million. This estimate is subject to change, as we remain exposed to general future valuation risk. Actuarial valuations will be required as of December 31, 2005, for all of our DB pension plans. Required funding levels for 2006 and beyond may change as a result of these updated actuarial valuations. If the return on plan assets, interest on the obligation, or actual experience of the plans are better or worse than initially anticipated, the valuations could result in either lower or higher minimum required contributions.

Higher cash contributions are gradually leading toward an improved going concern funding position for the DB pension plans. As this occurs, we are shifting the asset mix and strategies in the pension plan funds to mitigate the impact that future interest rate changes and investment returns will have on the plans' funding position. As well, all of our DB pension and OPEB plans are now closed to new entrants, placing a cap on the future growth of these obligations.

Reliance on systems

We are reliant on our systems as they enable us to provide services to customers, manage customer relationships, billings and inventory. They also support many other vital activities. These systems are made up of many integrated parts consisting of cable, equipment, buildings and towers, IT equipment, IT software and the related data. Our operations depend on how well we protect these components against damage from fire, natural disaster, power loss, hacking, computer viruses, disabling devices, deliberate acts of vandalism, acts of war or terrorism, and other events. Any of these events could cause our operations to be shut down indefinitely. Our systems are connected with the systems of other telecommunications carriers, and we rely on them to deliver some of our services. Any of the events mentioned previously, as

well as strikes or other work disruptions, bankruptcies, technical difficulties or other events affecting the networks of these other carriers, could hurt our business, including our customer relationships and operating results.

Changing technology

We operate in an industry that experiences constant change, driven by rapid advances in technology, evolving industry standards, customer demands and short product life cycles. Our success is dependent on our ability to anticipate and respond to these changes in order to effectively deliver new services and technologies to our customers.

There is a risk associated with adopting new technologies to serve our business needs. New technologies invested in may have shorter than anticipated product life cycles due to evolving standards or sudden advances in the development of competing products or services. This may result in increased re-engineering costs to incorporate new technology and may cause current products or services to become unmarketable or could cause prices to fall, resulting in a negative financial impact.

We are continuing the evolution of our network from a circuit-based technology infrastructure to an IP infrastructure. This evolution enables the development of enhanced services for our customers through the integration of voice, data and video. This integration plays a significant role in increasing operating and capital efficiency. In some cases, significant investments need to be made before it can be determined if the new services will be successful in the marketplace. There is no assurance that customers will adopt these new services or migrate from existing services in a reasonable period of time.

The adoption of new IP-based services may be influenced by the customer perception of the security, reliability and quality of IP networks. There are no assurances that solutions will be available to allow service providers to totally defend customers against all forms of computer viruses and attacks.

We are responding to the fast pace of technological change by embracing new service development with strategic partners, accelerating new service introduction and developing an integrated growth plan to remain a next generation services provider. The success of new products is influenced by a number of factors, not all of which are under our control. Considerable effort is expended to ensure we correctly interpret, predict and respond to changes in technology, the regulatory environment, partner relationships and customer demand. However, we are not immune to sudden or unanticipated changes in any of these areas. This may result in the failure of new services and products to meet expectations and result in lower than anticipated net income.

Increasing competition

Atlantic Canada continues to be among the most competitive telecommunications markets in North America for local residential service. Our Atlantic Canadian population and economy are growing slowly compared to the rest of the country, yet our competitors are among the largest, nationally and internationally. In our business market, we compete with traditional telecommunication operators that are commoditizing communications services and also with

international system integrators offering consulting and solutions, based on in-depth vertical knowledge learned elsewhere.

Our focus is on building trust-based relationships with our customers and collaborating with them to make their businesses successful. Our strategy includes enhancing our services and packages to create compelling value, innovating with our customers to provide complete integrated ICT solutions, improving our cost structure to enable greater price competitiveness, and expanding our IP network and its capabilities to provide broader access and innovative solutions. Competition, and particularly changes in the competitive landscape, can place these strategies at risk, and as such have a negative impact on future revenue growth and profitability. In recognition of this we constantly monitor our marketplace and respond accordingly to ensure we maintain our leadership position.

Local and long distance

In 2006, it is expected that a new competitor will begin to offer local telephone service in a large portion of our marketplace. This competitor will have the ability to offer four-services bundles, consisting of telephone, Internet, wireless and TV. Cable competitors are free from regulation and are able to offer local service in bundles at greatly reduced prices in a bid to gain market share. We are vigilant and passionate about our customers and continue to pursue them with compelling value packages, offering value, simplicity and competitive pricing. However, there is no assurance that this will mitigate churn and market share erosion resulting from new competitive entrants to our marketplace.

In addition to cable competitors in our local service market, a threat to our customer base continues to be the slow and gradual replacement of local landline service with wireless-only service. This puts pressure on revenues for local service and also leads to declining revenues for services and features that are carried on the local network, including Internet and long distance.

The value of long distance as a stand-alone service has diminished but it is an integral component in the customer solution. In the telecommunications industry, long distance is increasingly offered within flat-rate calling plans while alternatives like VoIP, instant messaging and peer-to-peer applications replace traditional calling, contributing to continued price and minute erosion. Competition continues with dial-around and prepaid card providers, traditional primary interexchange carrier competitors and resellers, and most recently, VoIP providers. VoIP will continue to erode traditional long distance as the technology improves and managed VoIP services are launched, making the technology transparent and more attractive to the consumer. We are currently conducting a VoIP technical trial and results will be integrated into our voice evolution strategy.

Wireless

National and international wireless providers dominate our landscape. Competitors are increasing their network coverage and dealer channel breadth while service offerings including reduced rates for local and long distance minutes, innovative applications and handsets are being promoted as the new differentiators. This activity results in constant pressure on our pricing and revenues. We expect intense competition to continue as the industry has forecasted continued growth in wireless penetration and application opportunities. While competitors

threaten our position in the market place, we continue to invest in our network, collaborate with our customers to provide innovative solutions, and present extensive, reliable coverage and customer service they can trust.

Internet

Internet penetration is still growing in our market. As IP becomes standard, we are experiencing an increasingly diverse and global group of competitors ranging from cable providers with excess network capacity to IT companies, equipment providers and system integrators that increasingly bundle telephony components and professional services into solutions at commodity prices. We are continually challenged by these competitors as they assert pressure on our pricing, revenues and market share. We will continue to build our ICT expertise and to serve our customers holistically, helping them evolve their networks and providing them with world-class industry-specific solutions.

Television

We are new entrants to the television market with our launch of Aliant TV, our IP-TV service. We launched this service in one area while offering our entire market the choice of satellite TV through Bell ExpressVu service. Cable TV penetrates the majority of our market and accounts for the majority of market share. While we are starting to gain market share with Aliant TV service, and the opportunity for growth is large in specific markets, Aliant TV service requires high-speed Internet and will be dependent on high-speed Internet-penetrated urban areas. Television is integral to home entertainment and to bundled packages. Through Aliant TV service we are offering customers the opportunity to be early adopters of an innovative, yet familiar, product.

Changing regulations

Overall regulatory environment

The business of our primary telecommunications company, Aliant Telecom Inc., is affected by decisions made by the CRTC. This has been a challenging year with several significant decisions being made by the Commission.

Our profitability continues to be negatively influenced by regulatory changes concerning the rates charged and the terms and conditions offered for price-regulated services. The outcome of future regulatory reviews could have an impact on our ability to compete effectively and our future revenues and costs.

Another important initiative that could affect our industry is the federal Industry Minister's announcement early in 2005 of a review of Canada's current telecommunications policy. We are hopeful that the outcome of the review will lead to policies that will allow incumbent telephone companies, such as Aliant Telecom Inc., to compete fairly and limit regulation to areas where it is proven to be needed.

Today the prices of telecommunications services offered by competitive local exchange carriers (CLECs) are free from rate regulation while many of our local and other telephone service rates continue to be regulated by the CRTC. Any change in the regulations governing these services can potentially affect us.

The CRTC is currently reviewing a number of items that could have a financial impact on our company. A decision on our application for forbearance from price regulation of local residential services in certain areas or exchanges in Nova Scotia and Prince Edward Island which would allow for greater pricing flexibility and symmetrical competition is expected in March, 2006. As well, we are expecting a decision shortly on our request that the CRTC exclude, for the reporting period of April to December 2004, below-standard work-stoppage-related results from the calculation of service quality related customer rebates. In 2006, we are also expecting the CRTC to provide a ruling on the magnitude and treatment of deferral accounts, which were established pursuant to the 2002 Price Cap Decision, and conduct a proceeding to review the regulatory regime that will be effective beyond the close of the current price cap period, which could affect our revenues and earnings in 2007 and beyond. We will also be faced with other challenges in 2006, including appealing the VoIP decision and implementing the CRTC's requirements for wireless number portability.

Local services forbearance application

In April 2004, we filed a forbearance application with the CRTC requesting them to stop regulating local residential phone service within certain areas of Nova Scotia and Prince Edward Island where there is significant local residential competition.

In addition to the forbearance request, we also asked for interim relief from certain restrictions on promotions and certain rates that required CRTC approval until the CRTC ruled on the framework for local service forbearance. In August 2004, the CRTC determined that our request for relief from the restrictions will be considered as part of a proceeding in which our request for forbearance for local service will be addressed.

On October 7, 2005, the formal process with regards to the CRTC proceeding on local forbearance was completed and a decision is expected in March 2006.

Quality of service rebates

In 2005, we filed applications requesting that the CRTC exclude from the calculation of service quality related rebates, certain below-level service standards associated with the labour disruption of our unionized workforce in 2004 and the residual effects of the lengthy work stoppage.

A decision from the CRTC related to our 2004 reporting period is expected in early 2006.

Deferral account

In the 2002 Price Cap Decision, the CRTC established deferral accounts. The CRTC created deferral accounts to address concerns that ILEC price decreases for residential services based on the price cap formula would negatively affect competition. Based on this rationale, the Commission ordered companies to put the amount that would otherwise have been granted as annual price reductions into this notional 'account'.

We have submitted to the Commission our proposed amount in our deferral account and have also filed a proposal to clear our deferral account balance. We have not recognized the deferral account as a liability in our financial statements, but a liability, should one arise as a result of the CRTC decision on our proposal, will be charged to operating income or capital

investments, as appropriate. We estimate that the deferral account balance as of December 31, 2005, could be between \$6 million and \$39 million.

A decision from the CRTC is expected in early 2006.

Current price cap regime extended

Current price cap rules that were scheduled to expire in 2006 under the CRTC Price Cap Decision of May 2002, have been extended for a period of one year to May 31, 2007. Prices for certain ILEC services will continue to be capped by an index calculated using a target productivity factor and an inflation measure. During years that inflation is lower than the target productivity factor, ILECs will be required to reduce certain retail prices.

The CRTC will begin a price cap review in the first half of 2006 after they have released their decision on local service forbearance. The CRTC decision based on this review could greatly affect us as well as our customers and competitors.

VoIP appeal

In conjunction with other Canadian ILECs, we filed a petition with the Governor in Council seeking a fundamental change to the Commission's VoIP decision. The petition emphasized the fact that VoIP is indeed a different service than traditional landline access service and that the Commission's approach to regulating VoIP would ultimately harm innovation and competition in Canada.

If the Commission's decision is not altered, we will be working in an environment in which we are subject to price-regulation while competitors are not. This would negatively affect our future revenue potential.

Wireless number portability

In December 2005, the CRTC issued its decision on the implementation of Wireless Number Portability, providing for the porting of telephone numbers between wireless carriers in Canada and between wireless and wireline services.

Certain wireless carriers are required to implement complete portability by March 14, 2007, while other carriers, including Aliant Telecom Inc., must be able to port-out numbers by March 14, 2007, with the ability to port-in by September 12, 2007. To accommodate this, our system modifications will likely require a single implementation plan, therefore we are working toward the delivery of full number portability by the earlier date.

This issue affects our customers and a number of our internal wireless and wireline systems. The timeframe for implementation will be very challenging.

Legal contingencies and changes in laws

We review all legal proceedings and make an assessment of the likelihood of a negative outcome and the estimated impact. Losses are accrued for when a potential loss is deemed probable and its impact can be reasonably estimated. However, pending or future litigation could still have a material and negative effect on our results of operations, cash flows and financial position in the period in which the judgment or settlement occurs. Significant legal

contingencies outstanding are presented in note 22 to our consolidated financial statements for the year ended December 31, 2005.

In addition, the adoption of new laws, changes in laws or changes in their interpretation, including changes in tax laws or rates, could materially or negatively affect our results of operations, cash flows and financial position.

Capital management risks

The financial transactions we participate in may expose us to credit, foreign currency, interest rate and financial instrument risks. A more detailed description of our exposure to these risks and the procedures in place to mitigate these risks is described in note 18 to our consolidated financial statements for the year ended December 31, 2005.

Disclosure controls and procedures

Under the supervision and participation of our management, including the chief executive officer and the chief financial officer, we evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Multilateral Instrument 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings) as of December 31, 2005. Based on that evaluation, the chief executive officer and the chief financial officer concluded that our disclosure controls and procedures are effective in making known to them material information relating to us and our consolidated subsidiaries required to be disclosed in our reports filed or submitted under the Multilateral Instrument.

Supplementary financial information

Consolidated quarterly financial information (unaudited)

For the eight quarters ended December 31, 2005

| (millions of dollars, except for per share amounts) | 2004 | | | | 2005 | | | |
|---|----------|----------|----------|----------|----------|----------|----------|----------|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 | Q4 |
| Total operating revenues | \$ 515.6 | \$ 508.7 | \$ 499.3 | \$ 509.9 | \$ 524.4 | \$ 517.3 | \$ 520.1 | \$ 534.9 |
| Net income | \$ 46.0 | \$ 40.2 | \$ 37.0 | \$ 7.5 | \$ 43.6 | \$ 49.8 | \$ 50.8 | \$ 55.2 |
| Preferred share dividends | 2.4 | 2.4 | 2.4 | 2.4 | 2.4 | 2.4 | 2.4 | 2.4 |
| Net income applicable to common shares | \$ 43.6 | \$ 37.8 | \$ 34.7 | \$ 5.1 | \$ 41.2 | \$ 47.4 | \$ 48.4 | \$ 52.8 |
| Basic and diluted earnings per common share | \$ 0.33 | \$ 0.28 | \$ 0.26 | \$ 0.04 | \$ 0.31 | \$ 0.36 | \$ 0.37 | \$ 0.41 |

Our 2004 results were affected by a labour disruption, which commenced on April 23 and concluded on September 20, and by the provision of an ERIP in December. The comparability of the 2005 operating results with 2004 is discussed in more depth throughout this document. The comparability of our operating results is also affected by the timing of telecommunications product sales and IT fulfillment sales that are typically large and sporadic in nature.

Consolidated annual financial information

For the years ended December 31

(millions of dollars except per share amounts)

| | 2005 | 2004 | 2003 |
|---|------------|------------|------------|
| Operating revenues | \$ 2,096.7 | \$ 2,033.5 | \$ 2,059.0 |
| Net income from continuing operations | \$ 199.4 | \$ 130.7 | \$ 188.6 |
| Net income from discontinued operations | - | - | 111.3 |
| Net income | \$ 199.4 | \$ 130.7 | \$ 299.9 |
| Basic and diluted earnings per common share | | | |
| Continuing operations | \$ 1.46 | \$ 0.91 | \$ 1.30 |
| Discontinued operations | - | - | 0.81 |
| Total basic and diluted earnings per common share | \$ 1.46 | \$ 0.91 | \$ 2.11 |
| Dividends declared per common share | \$ 1.18 | \$ 1.10 | \$ 1.08 |
| Dividends declared per preferred share | \$ 1.36 | \$ 1.36 | \$ 1.36 |
| Total assets | \$ 2,866.9 | \$ 2,903.6 | \$ 3,004.4 |
| Total long-term debt (including current portion) | \$ 904.5 | \$ 896.4 | \$ 990.1 |

In 2003, several segments were reported as discontinued operations and sold during the year. The 2004 results were affected by a labour disruption, the provision of an ERIP and business acquisition and divestiture activity. As well, pension and OPEB costs were significantly higher in both 2004 and 2005 than 2003. The comparability of 2005 with 2004 operating results is discussed in more depth throughout this document.

Forward-looking statements

This MD&A contains forward-looking statements related to our future financial condition and results of operations. These statements are based on current expectations and estimates about the markets in which we operate and management's beliefs and assumptions regarding these markets. In some cases, forward-looking statements may be identified by words such as "anticipate", "believe", "could", "expect", "plan", "seek", "may", "intend", "will" and similar expressions. These statements are subject to important risks and uncertainties, which are difficult to predict, and assumptions, which may prove to be inaccurate. Some of the factors which could cause results or events to differ materially from current expectations include but are not limited to: general economic conditions; stock market volatility; market or business conditions; the changing competitive environment; changing regulatory conditions or requirements; changing technology; changing discount rates and market returns on pension plan investments; our ability to achieve strategies and plans; and our success in implementing productivity initiatives. Some of these factors are largely beyond our control. Should any factor affect us in an unexpected manner, or should assumptions underlying the forward-looking statements prove incorrect, the actual results or events may differ materially from the results or events predicted. All of the forward-looking statements made in this document and the documents referred to within are qualified by these cautionary statements. There can be no assurance that the results or developments anticipated by us will be realized or, even if

substantially realized, that they will have the expected consequences for us. Readers should not place undue reliance on any forward-looking statements.