rom: Russ Korins, Subject: what do you feed these people? what do you feed your
taff? They are superhuman. It is not merely that my own experiences with them
ave been amazing. Everywhere I look in the newsgroups, people are raving about
special phone call here, a prompt call back there, a polite email there, and
o on. It is simply stunning.Good luck and best wishes for the future -- still
heering for MindSpring! From: "Jerry R. Daniel" , My congratulations to all of
ou folks at MindSpring...I tried one of the other national services for a trial
eriod while I was setting up my account with MindSpring. I have now canceled
ith the other service because I am so pleased with your service. From my first
ontact with one of your sales representatives who cheerfully answered all of my
uestions to your helpful and patient tech support people, I have been more than
leased with your entire operation. Congratulations on a great job. I am telling
ll of my friends how satisfied I am with MindSpring. I am proud to be a member
f the finest net service in the nation. From: Robert Krausankas , Subject:
udo's for MindSpring! Just a note to "pat you folks on the back" for a job well
one. I couldn't begin to list the providers I have been thru over the last 3
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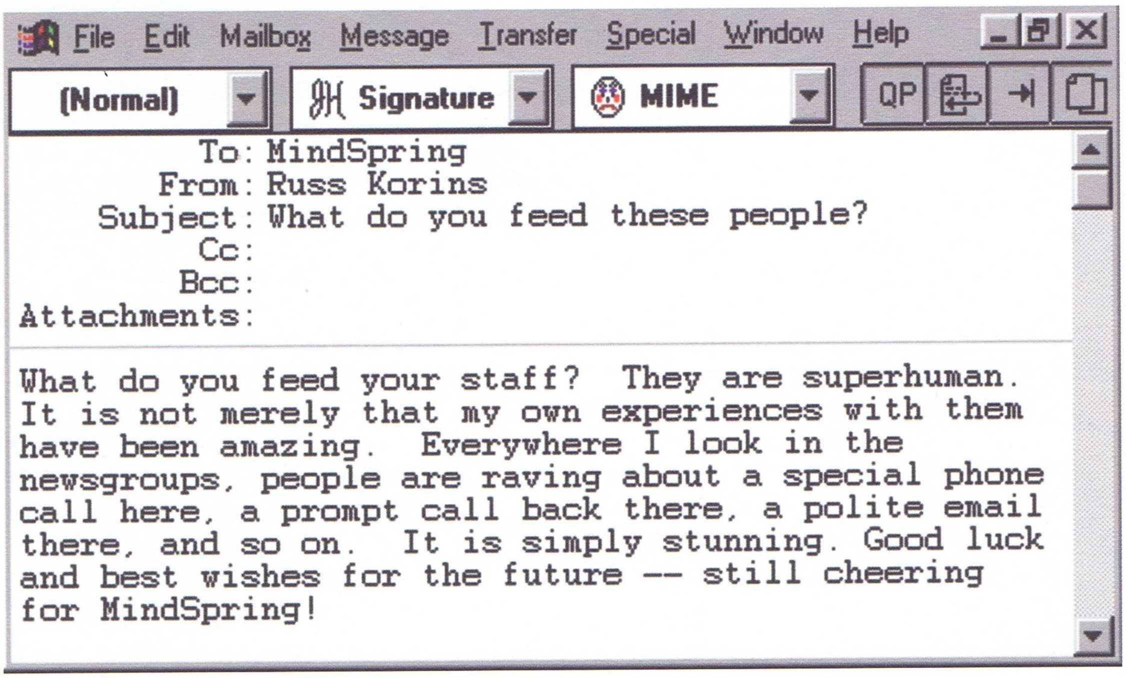

he money they spend with MindSpring is good value...Your customers really like
oing business with you, want you to succeed, and feel they are elite because
hey are MindSpring customers. That's a special feeling to have created, and they
ant you to keep it up. All of which is to say, if I'm any judge, you are win
ing the war "out in the tall grass." Cheers! Paul Scheele I was helped by
erson today in tech support... who went the extra mile. I have been in sales
nd customer service for many years and I take notice of people in their jobs
little more than the average bear. He was very helpful and understanding, a
am a novice...I think you guys need to write a book on hiring correct peopl
n the business world. Thanks for the great service and support. Bryan Y
ritchard From: Mel Stewart, Subject: Sign-up, Thanks for your company's fas
esponse. After waiting on AT&T for two months, I decided to abort that and sig
p with you. I was pl days I had the startu
ackage in my snailmai sily MindSpring set u
n my machine. I hac From: "Christopher D
ancette", Subject: yo ed to drop you a quic
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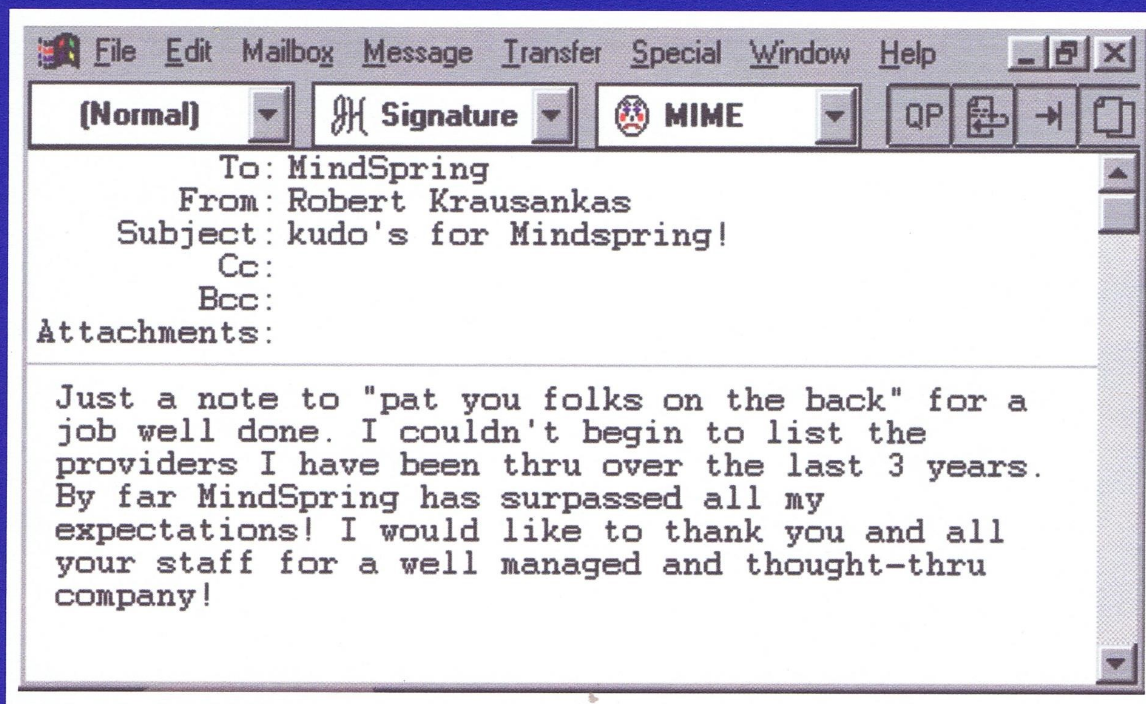
ad it. From the momer .. I could tell I wa
n good hands...The sales people were great. The software took all of five min
tes to install. And then I got in without fail every time I tried and have logge

MindSpring

1996 Annual Report

<mindspring.com>



To: MindSpring
From: Robert Krausankas
Subject: kudo's for Mindspring!
Cc:
Bcc:
Attachments:

Just a note to "pat you folks on the back" for a job well done. I couldn't begin to list the providers I have been thru over the last 3 years. By far MindSpring has surpassed all my expectations! I would like to thank you and all your staff for a well managed and thought-thru company!

MindSpring is a leading national Internet service provider, specializing in serving individual subscribers. We are building a brand image with a unique reputation for quality in our industry. As of December 31, 1996, the Company provided nationwide Internet access through approximately 218 points of presence and served approximately 118,000 Internet access subscribers and approximately 3,700 Web Hosting customers.

Purpose:

To change the way the world does business by demonstrating that a company based on integrity and respect for the individual can do an outstanding job of serving its customers, providing meaningful work for its employees, delivering an exceptional return to its owners, and being a force for good in its community.

The Company has been guided by and has striven to achieve its Purpose since its inception and is committed to continuing to work toward these goals.

Core Values and Beliefs

- We respect the individual, and believe that individuals who are treated with respect and given responsibility respond by giving their best.
- We require complete honesty and integrity in everything we do.
- We make commitments with care, and then live up to them. In all things, we do what we say we are going to do.
- Work is an important part of life, and it should be fun. Being a good business person does not mean being stuffy and boring.
- We are frugal. We guard and conserve the company's resources with at least the same vigilance that we would use to guard and conserve our own personal resources.
- We insist on giving our best effort in everything we undertake. Furthermore, we see a huge difference between "good mistakes" (best effort, bad result) and "bad mistakes" (sloppiness or lack of effort).
- Clarity in understanding our mission, our goals, and what we expect from each other is critical to our success.
- We are believers in the Golden Rule. In all our dealings we will strive to be friendly and courteous, as well as fair and compassionate.
- We feel a sense of urgency on any matters related to our customers. We own problems and we are always responsive. We are customer driven.

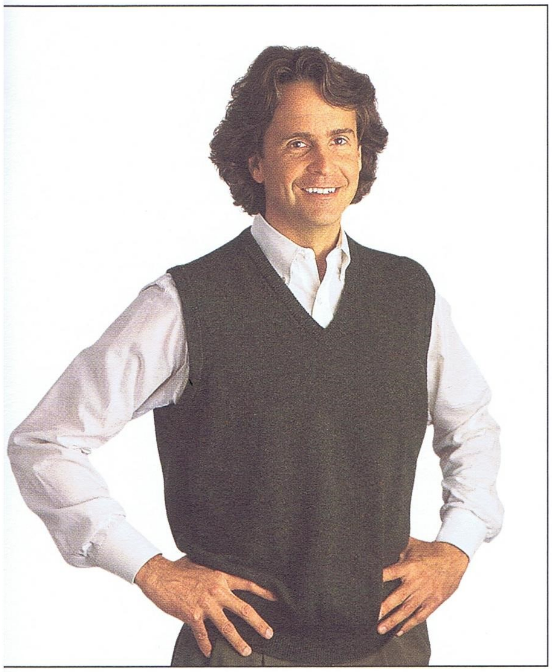
1996. What a year! MindSpring became a public company in March, and we completed a second public stock offering in October. Our subscriber base grew over 880% during the year. Our revenue grew over 700%. We acquired the individual subscriber bases of two major competitors, and several smaller ones. We increased our staff from 95 to 321. We grew from a regional provider to a national provider. And, in the midst of all of this extraordinary growth and activity, we believe we have consistently maintained the highest service quality and customer satisfaction of any significant competitor in our industry.

What A Year!

MindSpring is one of literally thousands of Internet service providers that have been formed since the beginning of 1994. Of all of the companies started in this market during this time, MindSpring has grown to be one of the largest. Of all of the companies with a significant number of subscribers in our industry, MindSpring is consistently rated at or near the top for quality and customer satisfaction. We have received PC World's "Best Buy" award, an "Excellent" rating from PC Magazine, the "People's Choice, Best Internet Service Provider" award from NetGuide, and a consistent top five ranking in CNET's survey. I invite you to ask, "Why?"

The most important thing about MindSpring has nothing to do with the Internet. It has nothing to do with computers. It has nothing to do with telephone systems. The most important thing about MindSpring is our philosophy, our values, and our determined effort to live up to these values. We don't want to be a typical company. We want to be different, and better. Our guide in this effort is the MindSpring Core Values and Beliefs, which you'll find printed on page 1. The CV&Bs, as we call them, describe how we aspire to behave. We are not perfect in our efforts to live up to this aspiration, nor will we ever be, but we do know what we are aiming for. Our quest to build a different and better kind of company based on these Core Values and Beliefs gives meaning to our work. It is our permanent central focus.

We see no conflict between doing the right thing and doing the profitable thing. We believe that in the long run they are identical. We believe that our focus on the Core Values and Beliefs is the way to maximize the creation of value for our owners. We are committed to doing that.



Despite our dramatic growth in the three years of our existence, MindSpring is still a relatively small company. We do not intend to stay small. Our company purpose, the reason MindSpring exists, is to change the way the world does business by demonstrating that a company based on integrity and respect for the individual can do an outstanding job of serving its customers, providing meaningful work for its employees, delivering a favorable return to its owners, and being a force for good in its community. We will only live up to that purpose by becoming a substantial enterprise. That is what we intend to do.

1997 will be an important year for us, as we continue on our path to profitability. In 1997, we will continue our efforts to:

Focus on individual subscribers
Capitalize on our superior customer service and support
Expand marketing opportunities and leverage national growth opportunities
Grow through acquisitions

On the following pages you'll read more about the specifics of our business, our strategies, and our financial results.

Thank you very much for your support.

Sincerely,

Charles M. Brewer
Chief Executive Officer
MindSpring Enterprises, Inc.

1996 Highlights

Revenue Growth

Revenues for 1996 were $18,132,000 vs. $2,227,000 in 1995, an increase of over eight-fold. Of this figure, access revenue was $13.4 million, start-up fees were $2.4 million, and business services (primarily web hosting) accounted for $2.3 million.

Subscriber Growth

We had approximately 121,800 subscribers at the end of 1996, vs. approximately 12,000 at the end of 1995. This includes approximately 118,100 Internet access customers and approximately 3,700 web hosting customers.

Acquisitions

In September we completed the acquisition of approximately 42,000 dial-up subscribers from PSINet, Inc. In addition, we signed an agreement with PSINet enabling us to lease capacity on their network of over 200 points of presence (POPs) nationwide. This was a key strategic acquisition for us for several reasons. It instantly changed us from a regional to a national provider, which opened up Original Equipment Manufacturer (OEM) marketing opportunities, and allowed our subscribers who travel to reach us in most local markets. It also created economies of scale which will help bring us to profitability.

We also made nine other acquisitions in 1996, including that of a key competitor, Nando.Net, in the Research Triangle Park area of North Carolina. We acquired approximately 4,500 dial-up subscribers from Nando.Net.

National Coverage

As a national provider, we were able to participate in national scale OEM and affinity group marketing. We entered into an arrangement with Microsoft to be bundled in Win95, and an agreement with Monorail Inc., an Internet-ready computer manufacturer, in which the Company's software is included on Monorail's personal computers.

1997 Strategy

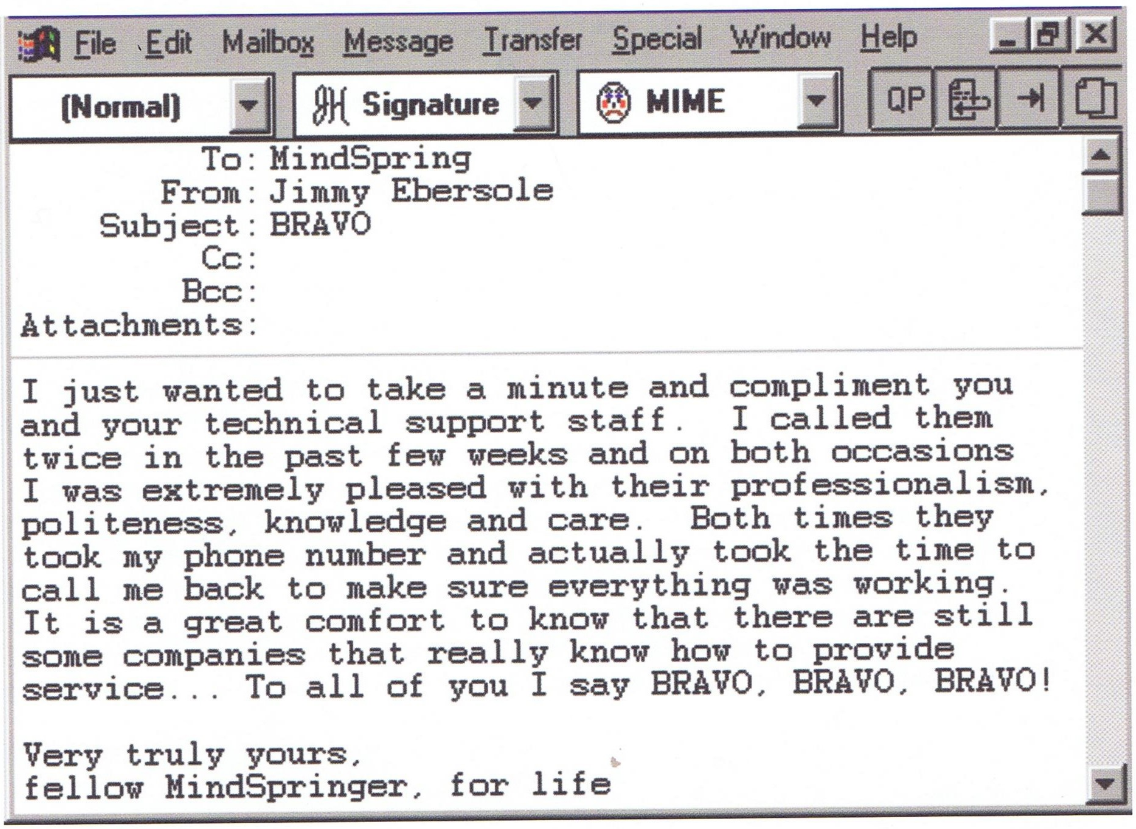
Focus on individual subscribers

We will continue to focus on individual subscribers.

This market segment is growing very rapidly, driven by increasing use of home computers and soon other Internet capable devices, and growing awareness of and demand for the Internet's resources. In our opinion, our competitors have been unsuccessful in delivering the

revenues up 700%

every time I've tried since -- and I'm a pretty heavy user. Your usage plans
e also perfect. To make things even better, I found out how polite and sup-
tive your technical support people were when I upgraded to The Works to get
econd mailbox...You also demonstrated great patience and understanding when I
led about other questions. (Your manual, by the way, is also considerably more
rough than I received from my previous servers.) I read in the paper today
t you are growing rapidly. You deserve it. If you continue to maintain your
es and keep up with the volume -- giving me hassle-free usage, I'm yours for
e. I'm a freelance writer and depend on my service for the vast majority of
communications (sending e-mail to editors, etc.). Compuserve almost put me out
business. MindSpring is increasing its potential. You are a model for the
ustry. All of us MindSpring customers owe you a great big "thank you" for
ng such a great job of adhering to your goals and standards throughout this
sive growth period. As always, the tech help people are doing their "front
e" best to be courteous and pleasant while assisting with problems. And your
vice just keeps on getting better. Thanks, Betty Griffin From: "Jerry D
tlock" , Subject: Unsolicited Testimonial, Over all you guys are doing a GREAT



ve been quickly and courteously remedied; rest assured that my referrals will
discontinue anytime soon. You are all to be commended on providing a much
eded service with seldom-seen efficacy. From: "Joseph Thomas", Subject
ndSpring Service, Well, it's Thanksgiving...how appropriate! Every once in
le, in conversations I've had about the Internet, someone says something abou
s problem or that problem -- not getting through, getting disconnected, slo
nnections, lack of technical support -- that reminds me how lucky I am to hav
pure chance) chosen MindSpring as my ISP. I always have the same answers fo
ese folks: "MindSpring is GREAT!" It's been a while since I've required tec
pport, but when I needed it there was always a bright helpful person to guid
. What's MORE impressive, to me, is that if that person felt uncertain abou
answer, he/she turned me over to someone that they felt may be better able t
lp me! (This must be something they've been trained to do -- the natural incli
tion for computer geeks is to try to figure things out for themselves withou
eking help from anyone!) I rarely have any trouble getting logged on, my dis

quality, service offerings and pricing that this market demands. We think this provides an excellent opportunity for us to continue to differentiate our service and attract subscribers. We believe that focusing primarily on this segment of the market makes it easier for us to deliver superior quality while still growing very rapidly.

Capitalize on our superior customer service and support -

Our job is not just to provide a functioning connection - it is to do everything we can to make sure our customers have a positive experience with MindSpring and the Internet.

Our customers - and the industry - recognize this commitment. We recently won PC World's Best Buy award. We are consistently ranked higher than any other significant competitor in C/NET's ratings of Internet service providers, which are compiled from actual customer responses. We ranked number one in InfoWorld's end user poll. We had the highest scores in PC Magazine's review of Internet service providers and Online service providers. We won the People's Choice Award for Best Internet Service Provider from NetGuide. In our own most recent annual survey, 92% of respondents said they were either satisfied or very satisfied with our overall service. Going forward, we will continue to focus on being the top quality provider.

Our starter kit is an important piece of the picture - it lets even novice net users get started with state of the art software tools and minimum hassle. In the upcoming months, our starter kit will move toward an integrated interface that provides an easy way to communicate with our subscribers using "push" technology. As a result of the introduction of this technology, our ability to update a subscriber's software quickly and reliably will improve, as will our ability to offer customized information to our subscribers such as local news, weather, personalized stock quotes and targeted messages. Our price plans provide an appealing option for all types of individual subscribers.

Our network itself is extremely important in making sure our customers have a positive experience. Our technologically advanced Network Monitoring Center has become a key competitive advantage for us. Our engineering group brings tremendous technical expertise to our team, and as a result, we believe enables us to stay on the leading edge. We are Beta testing US Robotics' X2 technology offering speeds up to 56Kbps, and will implement this new technology in 1997 in selected markets.

Our Customer Service and Technical Support groups continue to provide what we call "Wow" support: our objective is that every time a customer, or a potential customer, comes in contact with us they come away from the experience thinking "Wow. Why can't all companies be like that?" In the PC World review, the writer commented, "MindSpring works well and is easy to use. The support people we talked to were among the friendliest, most helpful we found." That, for us, was a home run.

subscribers up 880%

e. I guess I've been on MindSpring almost 2 years, and I've seen the place
w, well, geometrically. Still, things seem to be the same. I still get con-
ted, my connection is still clean, and based on what I've heard from other
dSpring customers, the support is still there. If you have time, please walk
und your building and give everyone a pat on the back for me -- hell, give
a big HUG for me! And don't leave yourself out -- to have a company grow the
MindSpring has grown, and to have consistent service throughout the growth -
ell, it's quite an accomplishment.Joseph Thomas From: David Ross, Subject:
! What an ISP, You guys are the greatest. Regardless if I email technical sup-
t or sales I always get an email promptly. I have been a user since I joined
Atlanta and now reside in NJ and the same service is always available. Never
usy signal. I am convincing everyone up here to jump on board. I am a tech-
al support and help desk analyst and work contract to set up the same. I wish
the desks I start end up like you guys. Keep up the great work!! You're the
t damn ISP in the nation. From: Martin Beeler, Subject: Accolades,I've been
remely UNhappy with several Internet providers to date. Naturally, I was skep-
al when I signed on with MindSpring as well! However...the customer service

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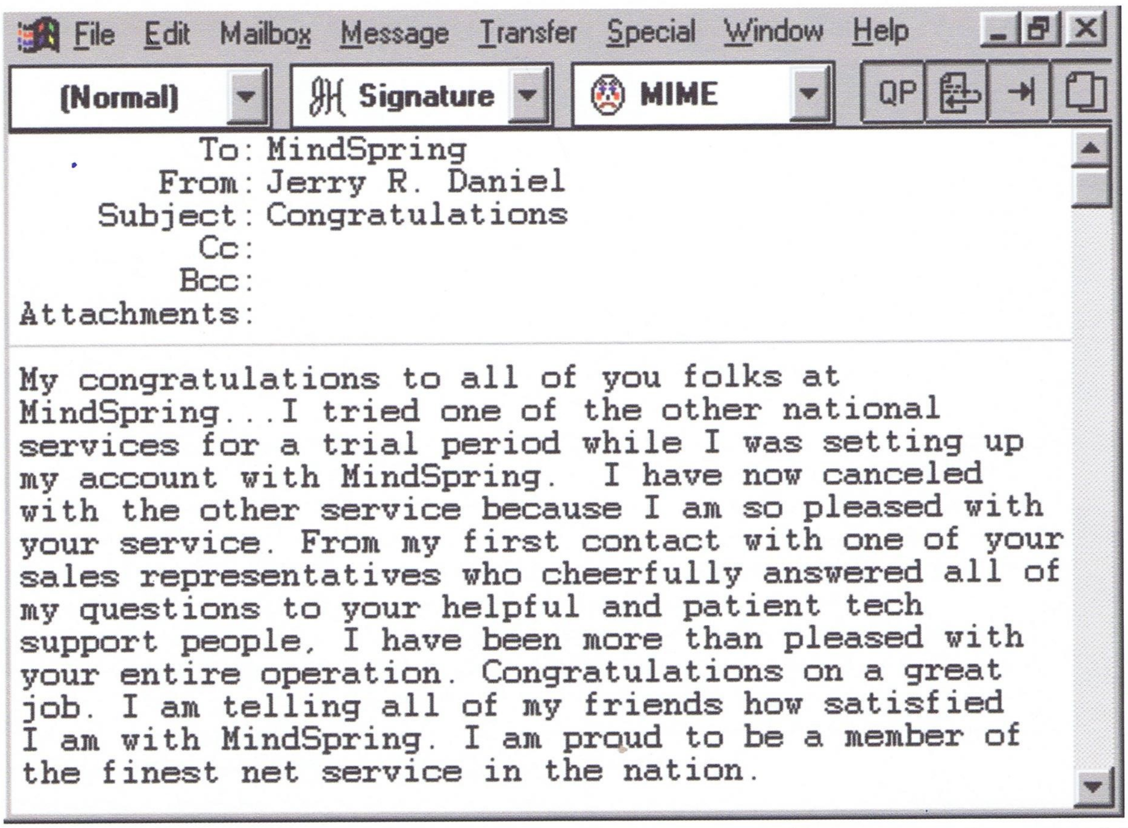

test. Well deserved. As a long time customer I fully agree. Your staff truly
resents the MindSpring Basic Beliefs.Your customer service is outstanding. I
always unhesitatingly recommend MindSpring whenever the subject of ISP's
es up. Best regards, Mike Conti Charles, my new "Wired" magazine just
ived. In the "Tired/Wired" column, AOL heads the "Tired" list, and--yes--
dSpring tops the "Wired" list. About time! I continue to refer scads of
sonal and business users to you. I just set up a corporate user with a
ain and loaded them up a web site (I work as a graphic designer); it was
eal pleasure because of the ease that your web group built in to your web
sting services. Take care. Great service. Peter Johnson A poem for the
h Support Rep who helped me last night...He was terrific, he was great, and
ever even had to wait. A late night call was all it took, I didn't have to
d the book. He found my missing file so quick, and reinstalled the soft-
e disk... configured preferences, got it started, then he quietly depart-
to leave me surf the net once more, IRQ, Telnet and explore. This compli-
t I hope you give him, and a place for him in tech heaven. Marilynn Huret

Expand marketing efforts; leverage national growth opportunities

We understand how to leverage our local marketing expertise to build density in selected markets. Density of customers in a particular locality is very important both from a gross margin perspective - a large POP is much more cost efficient than a small one - and also in terms of effectiveness of marketing, word of mouth, and referrals. Our marketing experience as a company is centered around this, and we plan to bring it to bear on selected additional markets - most notably, in 1997, New York City.

We will continue to develop our OEM opportunities by bundling our software with books, modems, and other third party products, pre-loading on computers, and selling through national retail chains. We are also exploring non-traditional channels such as Wolf Camera stores and national bookstore chains. Finally, we are exploring new ways to create partnerships and alliances to deliver service to our customers.

Grow through acquisition

MindSpring is well positioned to pursue additional acquisitions. With one big, one medium sized, and several smaller acquisitions under our belt, we believe we are well qualified to act as a consolidator in this business.

We are confident that there will be a number of target candidates and favorable acquisition pricing as other participants in the industry focus on things other than serving individual customers. Many Internet service providers have in the past simply defined themselves as "Internet Companies", doing a variety of Internet related work. These companies are very frequently narrowing their focus to something other than providing Internet access to individual customers and are looking for a good home for their dial-up subscribers. We believe we have positioned ourselves to be a consolidator in this business.

Profitability Drivers

Currently our top strategic priority is attaining our profitability goals. There are three major drivers helping us in our push towards profitability.

One driver is economies of scale. Our requirements in departments like Management Information Systems, Network Operations, and Administration do not scale up in a linear fashion with our revenue and subscriber base. By expanding our subscriber base, we are able to more efficiently utilize the capacity of these resources.

Another driver is the changing ratio of new customers to the installed base of customers. Our costs in sales and marketing and support are driven much more by the number of new subscribers than the number of existing subscribers. As our existing subscriber base grows and the ratio of new subscribers to existing subscribers drops, expenses as a percent of revenue can be expected to drop.

Ultimately, profitability and the overall success of our company depend on the third driver, our employees. It is their talent in the areas of technical skill, customer attentiveness, and business acumen that truly sets us apart in this industry.

The following table sets forth selected financial and operating data for the Company. The selected historical statements of operations data for the years ended December 31, 1996 and 1995 and for the period from February 24, 1994 (inception) to December 31, 1994 (the "Inception Period"), and the selected historical balance sheet data as of December 31, 1996 and 1995 have been derived from financial statements of the Company, which have been audited by Arthur Andersen LLP, independent public accountants, whose report with respect thereto is included elsewhere in this report. The selected historical financial and operating data set forth below should be read in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations," the Company's financial statements and notes thereto and other financial and operating data included elsewhere in this report. Dollar amounts (except per share data) are shown in thousands.

	Year Ended December 31, 1996	Year Ended December 31, 1995	Inception Period
Statements of Operations Data:			
Revenue	$ 18,132	$ 2,227	$ 103
Cost and expenses:			
Selling, general and administrative	14,161	2,230	121
Cost of revenue	8,208	966	52
Depreciation and amortization	3,285	265	5
Total costs and expenses	25,654	3,461	178
Operating loss	(7,522)	(1,234)	(75)
Interest expense, net	(90)	(725)	0
Net Loss	$ (7,612)	$ (1,959)	$ (75)
Per Share Data:			
Net loss per share	$ (1.45)	$ (0.62)	
Weighted average common shares outstanding	5,252,611	3,175,376	
Operating Data:			
Approximate number of subscribers at end of period	121,794	12,410	1,000
Number of Company employees at end of period	321	95	8
Balance Sheet Data:			
Working Capital	5,520	(3,099)	
Property and equipment, net	11,583	3,539	
Total assets	35,232	4,845	
Total liabilities	9,825	4,363	
Accumulated deficit	(9,646)	(2,034)	
Total stockholders' equity	25,407	482	

Overview

MindSpring is a national provider of Internet access. The Company was incorporated in Georgia on February 24, 1994, and began marketing its services in June 1994. The Company reincorporated in Delaware in December 1995. Prior to the PSINet Transaction in June 1996, MindSpring was a regional Internet access provider that offered its services through 40 POPs in the southeastern United States and had grown to approximately 34,500 subscribers.

On June 28, 1996, the Company entered into a Purchase Agreement (as amended, the "Purchase Agreement") with PSINet, pursuant to which the Company agreed to acquire certain of the tangible and intangible assets and rights related to the consumer dial-up Internet access services provided by PSINet in the United States, including (i) certain of PSINet's individual subscriber accounts, and (ii) the lease for the Harrisburg Facility and all related telephone switches and other equipment (the "Assets").

On June 28, 1996, the Company acquired 15,000 subscriber accounts from PSINet for $1,000,000 in cash and a $2,000,000 one-year promissory note (the "First PSINet Note"). The Company acquired an additional approximately 27,000 subscriber accounts and approximately $1,129,000 in related assets, including the Harrisburg Facility, as of September 1, 1996, at which time the Company issued an additional one-year promissory note to PSINet in the amount of $9,929,000 (the "Second PSINet Note"). The Purchase Agreement required the Company to apply 50% of the net proceeds from a public offering of the Company's Common Stock in October 1996 (the "October Offering") to repay amounts outstanding under the First and Second PSINet Notes. Accordingly, on October 21, 1996, the Company paid PSINet approximately $9,175,000, which consisted of (i) payment in full of the First PSINet Note, including the original principal balance of $2,000,000 plus a $100,000 (5%) principal increase pursuant to the terms of the First PSINet Note, and approximately $70,000 of accrued interest and (ii) partial payment of the Second PSINet Note in the amount of approximately $6,851,000 of principal (of the $9,929,000 total) and approximately $154,000 of accrued interest.

Effective as of January 24, 1997, the Company and PSINet further amended the Purchase Agreement to, among other things, fix an aggregate purchase price for the Assets in an amount equal to $12,929,000 (excluding accrued interest and increases in principal amount under the First and Second PSINet Notes previously paid by the Company)(the "Purchase Price"). In connection with fixing the aggregate amount of the Purchase Price, the Company and PSINet amended the Second PSINet Note to, among other things, reduce the principal amount owed thereunder to $3,078,324, an amount equal to the remaining balance of the Purchase Price as of January 24, 1997. As amended, the Second PSINet Note no longer accrues interest and is payable over a two year period.

In connection with the PSINet Transaction, the parties also entered into the Services Agreement which enables MindSpring to offer nationwide Internet access through PSINet's network of over 200 POPs. Pursuant to the Services Agreement, PSINet has agreed, among other things, to provide to the Company: (i) Internet connection services which meet reasonable commercial standards, including with respect to access and reliability; and (ii) access to PSINet's network monitoring systems and subscriber log-in and accounting information. The term of the Services Agreement is five years, commencing on June 28, 1996, and is automatically renewable annually thereafter unless either party notifies the other in writing not less than 12 months prior to the end of such five-year period or any 12-month extension thereof. Subject to certain exceptions, PSINet may not terminate the Services Agreement prior to October 31, 1998 and the Company may terminate the Services Agreement at any time upon 60 days' written notice to PSINet without penalty.

The Company and PSINet amended the Services Agreement effective January 1, 1997 to provide for certain discounts to the monthly service fees which otherwise would have been payable by the Company to PSINet. Such discounts could equal in the aggregate up to $4,150,000 through October 1998. The following table outlines the maximum discounts per month in network services fees that are available under the Services Agreement. The discounts will be reflected as reductions of cost of revenue in 1997 and 1998 to the extent earned.

Period	Discount Per Month
January 1997-July 1997	$ 150,000
August 1997-September 1998	200,000
October 1998	300,000

On August 6, 1996, the Company and The News and Observer Publishing Company ("N&O") entered into a definitive agreement, which was amended and restated on September 11, 1996, pursuant to which the Company agreed to acquire certain individual dial-up subscriber accounts in North Carolina in connection with N&O's Nando.net Internet access business (the "Nando.net Transaction"). The Nando.net Transaction was consummated on December 31, 1996. The number of subscribers acquired through the Nando.net Transaction was approximately 4,500 for approximately $519,000.

The Company derives revenue primarily from monthly subscriptions and start-up fees from individuals for dial-up access to the Internet. Monthly subscription fees vary by billing plan. In May 1996, in response to a changing competitive environment, the Company introduced five different pricing plans for dial-up access (one of which was discontinued in September 1996 due to low subscriber interest), compared to the two prior plan offerings. With the new pricing plans, new and existing customers have a choice of two "flat rate" plans (The Works and Unlimited Access) and two "usage-sensitive" plans (Standard and Light). These plan changes generally represent a reduction from the previous rates. The Company anticipates that additional price changes may be necessary in the future due to the dynamic nature of the Internet access industry. Management believes that the reduction in revenue per subscriber due to the effected price changes will be offset in the near term by continuing increases in subscriber growth. However, there can be no assurance that growth in the Company's revenue or subscriber base will be able to achieve or sustain profitability or positive cash flow.

For the year ended December 31, 1996, the average monthly recurring revenue per dial-up subscriber was approximately $21 (monthly recurring revenue plus usage charges for non-"Flat Rate" subscribers, divided by total subscribers), compared to $23 per dial-up subscriber for the year ended December 31, 1995. The decrease in revenue per subscriber is primarily the result of the aforementioned price changes implemented in May 1996. Start-up fees for new subscribers vary depending upon the promotional method by which the subscriber is acquired, ranging from $0 to $25. Aggregate subscriber fees are sufficient to cover the aggregate costs of direct materials, mailing expenses, and licensing fees associated with new subscribers. Most of the Company's individual subscribers pay their MindSpring fees automatically by preauthorized monthly charges to the subscriber's credit card.

In addition, the Company earns revenue by providing Web-hosting services, full-time dedicated access connections to the Internet and domain registration primarily to businesses and some individual subscribers. The Company's Web-hosting services allow a business or individual to post information on the World Wide Web, so that the information is available to anyone who has access to the Internet. Through its domain registration services, the Company provides subscribers the ability to personalize electronic mail addresses. These services have been classified as business services in the condensed statements of operations and the results of operations table below.

The Company's costs include (1) costs of revenue that are primarily related to the number of subscribers, (2) selling, general and administrative expenses that are associated more generally with operations, and (3) depreciation and amortization, which are related to the size of the Company's network and the deferred costs associated with acquired customer bases. Cost of revenue consists primarily of the start-up expenses for each subscriber, certain monthly licensing fees, and the costs of telecommunications facilities necessary to provide service to subscribers. Start-up expenses for each subscriber include one-time license fees paid to third parties for the right to bundle other capabilities into the Company's software, cost of diskettes and other product media, manuals, and packaging and delivery costs associated with the materials provided to new subscribers. The Company does not defer any such subscriber start-up expenses. Cost of revenue also includes monthly license fees per subscriber for the right to receive and make available certain news services. Telecommunications costs include the costs of providing local telephone lines into each POP, costs relating to the Services Agreement with PSINet for use of its network, and costs associated with leased lines connecting each MindSpring-owned POP to the Company's hub and connecting the hub to the Internet backbone. The Internet backbone consists of high-speed networks that link the smaller, independent networks of the Internet.

Selling, general and administrative costs are incurred in the areas of sales and marketing, customer support, network operations and maintenance, engineering, accounting and administration. Selling, general and administrative costs will increase over time as the Company's scope of operations increases. However, the Company expects that such costs will be more than offset by anticipated increases in revenue attributable to overall subscriber growth. In addition, significant levels of marketing activity may be necessary in order for the Company to build or increase its subscriber base in a given market to a size large enough to generate sufficient revenue to offset such marketing expenses. The Company does not defer any start-up expenses related to entering new markets. The costs associated with the development and registration of the Company's trademarks have been expensed as incurred. Such costs have not been material.

Prior to the PSINet Transaction, as the demand for the Company's services in a particular POP had grown, the Company had been required to invest in additional telecommunications equipment and provide additional local telephone lines for that POP. The Services Agreement provides the Company the option to evaluate on a POP-by-POP basis whether to continue to develop MindSpring POPs using the Company's capital resources or to conserve capital through utilization of PSINet POPs for a specified fee. As the Company expands into new markets, both cost of revenue and selling, general and administrative expenses will increase. To the extent the Company opens MindSpring POPs in new markets, such expenses may also increase as a percentage of revenue in the short term after a new MindSpring POP is opened because many of the fixed costs of providing service in a new market are incurred before significant revenue can be expected from that market. However, to the extent that the Company expands into new markets by using PSINet POPs instead of opening its own POPs, the Company's incremental monthly recurring costs will consist primarily of the fees to be paid to PSINet based on revenue per subscriber served, as provided in the Services Agreement. The margins on such subscribers will initially be higher than if the Company had developed its own POP in new markets.

The Company had 40 Company-owned POPs as of December 31, 1996, which were serving approximately 68,000 subscribers as of such date. In addition, the Company had access to PSINet's nationwide network of over 200 POPs. As of December 31, 1996, the Company and PSINet maintained approximately 18 POPs in the same service areas. Pursuant to the Services Agreement, the Company has the flexibility to offer Internet access in such overlapping POP locations through a MindSpring POP, through a PSINet POP or a combination of both. The Company does not currently plan to open a significant number of new MindSpring POPs during 1997. Management will, however, evaluate on a POP-by-POP basis the closing or expansion of existing MindSpring POPs or the opening of new MindSpring POPs based on subscriber demand and strategic considerations.

The Company has experienced operating losses since its inception as a result of efforts to build its network infrastructure and internal staffing, develop its systems, and expand into new markets. The Company expects to continue to focus on increasing its subscriber base which will result in higher expenses, but believes that the development of its operations will provide certain economies of scale which will decrease its cost of start-up fees, selling expenses, and general and administrative expenses as a percentage of revenue in the future.

RESULTS OF OPERATIONS

The following table sets forth certain financial data for the years ended December 31, 1996 and 1995 and the period from February 24, 1994 (inception) to December 31, 1994 (the "Inception Period"). Operating results for any period are not necessarily indicative of results for any future period. Dollar amounts (except per share data) are shown in thousands.

Results of Operations

	Year Ended December 31, 1996		Year Ended December 31, 1995		Year Ended 1994	
	(000's)	% of Revenue	(000's)	% of Revenue	(000's)	% of Revenue
Statements of Operations Data:						
Revenue						
Dial-up access to Internet	$13,420	74	$ 1,455	65	$ 70	68
Start-up fees	2,426	13	512	23	33	32
Business services	2,286	13	260	12	0	0
Total revenue	18,132	100	2,227	100	103	100
Cost and expenses:						
Selling, general and administrative	14,161	78	2,230	100	121	117
Cost of revenue-recurring	6,332	35	627	28	37	36
Cost of revenue-start-up fees	1,876	10	339	15	15	15
Depreciation and amortization	3,285	18	265	12	5	5
Total costs and expenses	25,654	141	3,461	155	178	173
Operating loss	(7,522)	(41)	(1,234)	(55)	(75)	(73)
Interest expense, net	(90)	(1)	(725)	(33)	0	0
Net Loss	(7,612)	(42)	(1,959)	(88)	(75)	(73)
Per Share Data:						
Net loss per share	$ (1.45)		$ (0.62)			
Weighted average common shares outstanding	5,252,611		3,175,376			
Operating Data:						
Approximate number of subscribers at end of period	121,794		12,410		1,000	
Number of Company employees at end of period	321		95		8	

Year Ended December 31, 1996 Compared to Year Ended December 31, 1995

Revenue: Revenue for the year ended December 31, 1996 totaled approximately $18,132,000, as compared to approximately $2,227,000 for the year ended December 31, 1995. The 714% increase in period revenue resulted primarily from an 881% increase in subscribers offset by a decrease in revenue per subscriber resulting from the price changes implemented in May 1996. Access revenue for the year ended December 31, 1996 represented 74% of revenue, as compared to 65% of revenue for the prior year. Subscriber start-up fees accounted for 13% of revenue for the year ended December 31, 1996, as compared to 23% for the year ended December 31, 1995. The Company anticipates that as its customer base continues to expand, subscriber start-up fees will progressively represent a smaller percentage of revenue. Business services revenue remained relatively constant as a percentage of total revenue.

Cost of revenue: For the year ended December 31, 1996, cost of revenue increased to approximately 45% of revenue as compared to approximately 43% of revenue for the year ended December 31, 1995. This increase is attributable to additional expenditures such as license fees and starter kits related to the PSINet Transaction and expenses associated with expanding the Company's network into 40 markets at the end of 1996 compared to seven markets at the end of 1995.

Selling, general and administrative expenses: Selling, general and administrative expenses were approximately 78% of revenue for the year ended December 31, 1996, compared to approximately 100% of revenue for the year ended December 31, 1995. The decrease in selling, general and administrative expenses as a percentage of revenue resulted from the Company benefiting from economies of scale with respect to such costs as salaries and wages that do not increase in direct proportion to increases in revenue and to cost control efforts implemented by management.

Depreciation and amortization: Depreciation and amortization expenses increased to approximately 18% of revenue for the year ended December 31, 1996, compared to approximately 12% of revenue for the same period in the prior year. The increase is attributable to the 257% increase in property, plant and equipment and the amortization of the acquired customer bases from the PSINet Transaction and the Nando.net Transaction. The Company is amortizing the costs of acquired customer bases over a three-year period. Amortization expense related to the acquired customer bases for the year ended December 31, 1996 was approximately $1,521,000.

Interest expense: The following table details the decrease in interest expense in 1996 versus 1995:

Event	1996	1995
Charge for Class C Convertible Preferred Stock	0	(637,000)
ITC Holding processing fee	0	(50,000)
Interest on PSINet notes	(324,000)	0
Net income (expense) - other	234,000	(38,000)
Interest (expense) income, net	$ (90,000)	$ (725,000)

Interest income increased in 1996 due to the increase in outstanding cash balances available for investment as a result of the proceeds from two public offerings. See "Year Ended December 31, 1995 Compared to Inception Period -- Interest Expense."

Year Ended December 31, 1995 Compared to Inception Period

Revenue: Revenues for the year ended December 31, 1995 were approximately $2,227,000, as compared to approximately $103,000 for the Inception Period. The Inception Period reflects sales activity from June through December 31, 1994. During the months of April and May 1994, the Company offered services to a limited number of subscribers on a "test" basis. The quarter ended September 30, 1994 was the first full quarter in which the Company made its services available to the general public. The increase in revenue in 1995 as compared to the Inception Period was primarily attributable to the Company being operational for the full 1995 period and the substantial increase in the number of subscribers in 1995.

Revenue for both periods was comprised of start-up fees and monthly service fees from subscribers. Access revenue accounted for 65% of total revenue in 1995, as compared to 68% in 1994. Subscriber start-up fees accounted for 23% of the total revenue in 1995, as compared to 32% in 1994. At December 31, 1994, the Company had approximately 990 dial-up subscribers, fewer than ten dedicated access subscribers and fewer than ten web-hosting service subscribers. At

December 31, 1995, the Company had approximately 11,830 dial-up subscribers, approximately 80 dedicated access subscribers and approximately 490 Web-hosting service subscribers.

Cost of revenue: For the year ended December 31, 1995, cost of revenue represented approximately 43% of revenue, compared to approximately 51% of revenue for the Inception Period. Cost of Revenue decreased as a percentage of revenue primarily as a result of economies of scale from higher utilization of telecommunications facilities.

Selling, general and administrative expenses: Selling, general and administrative expenses represented approximately 100% of revenue for the year ended December 31, 1995, compared to approximately 117% of revenue for the Inception Period. The decrease in selling, general and administrative expenses as a percentage of revenue resulted from the Company benefiting from economies of scale with respect to such costs as salaries and wages that do not increase in direct proportion to increases in revenue and cost control efforts implemented by management.

Depreciation and amortization: During the Inception Period, the Company had a very small asset base, which expanded dramatically during 1995. Consequently, depreciation and amortization expenses increased as a percentage of revenue to approximately 12% of revenue for the year ended December 31, 1995, compared to approximately 5% of revenue for the Inception Period.

Interest expense: In August 1995, ITC Holding Company, Inc. ("ITC Holding"), agreed to lend to the Company up to $2,000,000 in aggregate principal amount for working capital, general corporate purposes, and to fund capital expenditures (the "First ITC Loan"). All amounts outstanding under the First ITC Loan were due and payable in full on or before December 15, 1995. At December 15, 1995, the Company had not repaid any amounts outstanding under the First ITC Loan. In consideration of ITC Holding's agreement not to exercise its rights and remedies upon such default under the First ITC Loan, the Company agreed to pay ITC Holding a $50,000 processing fee, which the Company recorded as a charge to interest expense in the fourth quarter of 1995. In addition, the Company issued to ITC Holding an immediately exercisable warrant to purchase 100,000 shares of Class C Preferred Stock at an exercise price of $0.01 per share. The Company recorded the $637,000 difference between the fair market value of the warrants, at $6.38 per share, and the exercise price, at $0.01 per share, as interest expense in the fourth quarter of 1995. In December 1995, ITC Holding agreed to lend to the Company up to $4,000,000 for working capital and to fund capital expenditures (the "Second ITC Loan"). The remaining $44,000 of interest expense recorded during the fourth quarter of 1995 represents interest on the two loans. No such credit facilities existed during the Inception Period. The First ITC Loan accrued interest at 11% per annum and the Second ITC Loan accrued interest at 14% per annum.

LIQUIDITY AND CAPITAL RESOURCES

The Company has not generated net cash from operations for any period presented. The Company has primarily financed its operations to date through public and private sales of equity securities and loans from its principal stockholders and PSINet. During 1996, the Company completed an initial public offering of its Common Stock (the "Initial Offering") and the October Offering, issuing 2,025,000 shares at a price of $8.00 per share and 2,250,000 shares at a price of $9.125 per share, respectively. The proceeds from the public offerings were approximately $32,500,000, net of underwriting discounts and expenses. Upon completion of the Initial Offering, the Company repaid all outstanding principal amounts loaned to the Company by ITC Holding, totaling $3,500,000 of principal balance and approximately $97,000 in interest. The Company used approximately $9,175,000 or 50% of the net proceeds from the October Offering to pay PSINet in conjunction with the PSINet Transaction. Total cash from financing activities for the year ended December 31, 1996 was approximately $32,570,000, a $28,936,000 increase over the same period in 1995.

The Company used approximately $20,844,000 in cash for investing activities during the year ended December 31, 1996 and approximately $3,724,000 during the year ended December 31, 1995. This investing activity primarily relates to the purchases of telecommunications equipment necessary for the provision of service to subscribers, the Harrisburg Facility and customer acquisition costs related to the PSINet Transaction and the Nando.net Transaction.

On October 14, 1996, the Company and Monorail Inc. ("Monorail"), an Internet-ready computer manufacturer, entered into an agreement (the "Monorail Agreement") pursuant to which the Company's software is to be included on the personal computers manufactured by Monorail. On November 5, 1996, pursuant to the Monorail Agreement, the Company paid $560,000 in cash to Monorail, which included a prepayment of $500,000 for the first 12,500 subscribers acquired by the Company pursuant to this agreement ($40 per subscriber) and $60,000 for estimated expenses incurred by Monorail to include the Company's software on its PCs. The software preparation cost was expensed in 1996. To the extent that more than 12,500 subscribers are acquired by the Company pursuant to the Monorail Agreement, the Company will be required to pay Monorail $40 per additional subscriber. To the extent that fewer than 12,500 subscribers are acquired by the Company as of May 31, 1997, Monorail will be required to reimburse the Company at the rate of $40 per subscriber by July 30, 1997 for the difference between 12,500 and the actual number of subscribers acquired. If Monorail adds additional Internet access providers to its personal computers, the Company, at its option, may require Monorail to reimburse the Company upon seven days notice for the difference between 12,500 and the number of subscribers acquired by the Company. As of December 31, 1996, less than approximately 200 subscribers had signed up for the service under the Monorail Agreement.

On July 15, 1996, the Company and BellSouth entered into a two-year agreement (the "BellSouth Agreement"), pursuant to which the Company agreed to purchase telecommunications services from BellSouth for a minimum of $2,000,000 in the first year, and, in the second year, a minimum of 90% of the amount billed to the Company during the first year. The Company may renew the BellSouth Agreement pursuant to two one-year renewal options. In the event the Company terminates the BellSouth Agreement prior to its expiration, the Company is required to pay BellSouth a termination fee, subject to certain exceptions, equal to 50% of the amounts billed to the Company during the 12 months preceding such termination.

As of December 31, 1996, the Company had cash on hand of approximately $9,653,000. The Company's significant capital commitments through 1997 include approximately $624,000 in principal related to the Second PSINet Note and capital expenditures estimated to be approximately $9,000,000. The Company anticipates that it will generate cash flows from operations in 1997. The impact of the BellSouth Agreement and the Service Agreement discounts discussed above are reflected in the expected operating cash flows. Any refund from the Monorail agreement is not reflected in these numbers.

The Company estimates that its cash and financing needs through 1997 will be met by cash on hand and cash flow from operations. However, any increases in the Company's growth rate, shortfalls in anticipated revenue, increases in anticipated expenses, or significant acquisition opportunities could have a material adverse effect on the Company's liquidity and capital resources and would require the company to raise additional capital from public or private equity or debt sources in order to finance operating losses, anticipated growth and contemplated capital expenditures. If such sources of financing are insufficient or unavailable, the Company will be required to modify its growth and operating plans in accordance with the extent of available funding and attempt to attain profitability in its existing markets (including those accessible pursuant to the Services Agreement). The Company may need to raise additional funds in order to take advantage of unanticipated opportunities, such as acquisitions of complementary businesses or the development of new products, or otherwise respond to unanticipated competitive pressures. There can be no assurance that the Company will be able to raise any such capital on terms acceptable to the Company or at all.

MindSpring

<Balance Sheets>
As of December 31, 1996 and 1995

	1996	1995
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 9,653,234	$ 424,834
Trade receivables, net of allowance for doubtful accounts of $385,945 and $45,563 at December 31, 1996 and 1995, respectively	1,996,613	519,280
Prepaids and other current assets (Note 2)	853,122	273,658
Inventory	116,545	45,415
Total current assets	12,619,514	1,263,187
PROPERTY AND EQUIPMENT:		
Computer and telecommunications equipment	11,509,165	3,594,528
Assets under capital lease	1,472,885	0
Other	565,503	199,968
	13,547,553	3,794,496
Less: accumulated depreciation	(1,964,231)	(255,560)
Property and equipment, net	11,583,322	3,538,936
OTHER ASSETS:		
Acquired customer base, net (Notes 2 and 3)	10,727,268	0
Other	302,273	42,677
Total other assets	11,029,541	42,677
	35,232,377	4,844,800
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Trade accounts payable	$ 1,954,276	$ 847,965
Network services payable-PSINet (Note 3)	1,305,152	0
Other accrued expenses	1,243,826	478,256
Telecommunications costs payable	900,674	200,349
Current portion of capital lease liability (Note 8)	656,252	0
Current portion of notes payable (Note 7)	623,922	0
Deferred revenue	415,881	336,027
Loan from preferred stockholder (Note 7)	0	2,500,000
Total current liabilities	7,099,983	4,362,597
LONG TERM LIABILITIES:		
Notes payable (Note 7)	2,042,742	0
Capital lease liability (Note 8)	682,571	0
Total long-term liabilities	2,725,313	0
Total liabilities	9,825,296	4,362,597
COMMITMENTS AND CONTINGENCIES (Note 8)		
STOCKHOLDERS' EQUITY (Note 4):		
Preferred stock; $.01 par value; 1,000,000 shares authorized and 0 shares issued and outstanding at December 31, 1996 and December 31, 1995, respectively	0	0
Class A convertible preferred stock, $.64 par value; 1,187,895 shares authorized, and 0 and 1,187,895 issued and outstanding at December 31, 1996 and December 31, 1995, respectively	0	744,575
Class B convertible preferred stock, $1.55 par value; 645,596 shares authorized and 0 and 645,594 shares issued and outstanding at December 31, 1996 and December 31, 1995, respectively	0	1,000,000
Class C Convertible preferred stock, $.01 par value; 5,000,000 shares authorized and 0 and 100,000 shares issued and outstanding at December 31, 1996 and December 31, 1995, respectively	0	638,000
Common stock, $.01 par value; 15,000,000 shares authorized and 7,477,084 and 1,267,304 issued and outstanding at December 31, 1996 and December 31, 1995, respectively	74,771	12,673
Additional paid-in capital	34,978,225	120,547
Accumulated deficit	(9,645,915)	(2,033,592)
Total stockholders' equity	25,407,081	482,203
	$ 35,232,377	$ 4,844,800

The accompanying Notes to Financial Statements are an integral part of these statements.

MindSpring

<Statements of Operations>
For the years ended December 31, 1996 and 1995 and for the period of inception (February 24, 1994) to December 31, 1994

	1996	1995	1994
REVENUES			
Access	$ 13,419,521	$ 1,454,497	$ 69,744
Subscriber start-up fees	2,426,070	512,257	33,662
Business services	2,286,484	260,090	0
Total revenues	18,132,075	2,226,844	103,406
COST AND EXPENSES			
Cost of revenues -- recurring	6,332,152	626,404	37,329
Cost of subscriber start-up fees.	1,875,470	339,369	14,517
General and administrative	10,072,347	1,650,979	115,035
Selling	4,088,727	579,123	6,341
Depreciation and amortization	3,285,436	264,683	5,245
Total operating expenses	25,654,132	3,460,558	178,467
OPERATING LOSS	(7,522,057)	(1,233,714)	(75,061)
INTEREST (EXPENSE) INCOME, NET	(90,266)	(724,817)	0
NET LOSS	($7,612,323)	($1,958,531)	($75,061)
NET LOSS PER SHARE	($1.45)	($0.62)	
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING	5,252,611	3,175,376	

The accompanying Notes to Financial Statements are an integral part of these statements.