RATEXCHANGE CORP
Form 10-Q/A
November 21, 2001

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q/A

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2001
Commission File No. 33-19139-NY

RATEXCHANGE CORPORATION
(Exact Name of Registrant as Specified in Its Charter)

Delaware	11-2936371
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer ID Number)
100 Pine Street, Suite 500, San Francisco, CA	94111
(Address of Principal Executive Offices)	(Zip Code)

Registrant's telephone number, including area code: (415) 274-5650

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. YES ___ NO _X_

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

18,278,174 shares common stock as of November 20, 2001
2,000,000 shares preferred stock, Series A, as of November 20, 2001

RATEXCHANGE CORPORATION
FORM 10-Q
FOR THE QUARTER ENDED SEPTEMBER 30, 2001

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

RATEXCHANGE CORPORATION
(A Development Stage Company)
CONSOLIDATED BALANCE SHEET

ASSETS	Sep
	(Un
Current assets	
Cash and cash equivalents	$
Accounts receivable (net of an allowance for doubtful accounts of $9,460 at September 30, 2001 and $4,960 at December 31, 2000)	

Investment securities available for sale	
Notes Receivable	
Interest receivable	
Prepaid expenses	

Total current assets	
Property and equipment (net of accumulated depreciation of $655,730 and $240,791 in 2001 and 2000)	
Other assets	
Investment in affiliate	
Deposits	

Total assets	$
	===

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities	
Accrued expenses and liabilities	$
Accounts payable	
Notes payable	

Total current liabilities	
Accrued Lease Liabilities	

Total Liabilities	
Stockholders' equity (deficit)	
Preferred stock, $.0001 par value, 60,000,000 shares authorized; 2,000,000 issued and outstanding issued and outstanding	
Common stock, $.0001 par value; 300,000,000 shares authorized; issued and outstanding: 18,053,000 shares in 2001 and 17,783,000 shares in 2000	
Additional paid-in capital	8
Accumulated deficit	(8
Deferred compensation	
Notes receivable on sales of common stock	
Accumulated other comprehensive loss	

Total stockholders' equity (deficit)	(

Total liabilities and stockholders' equity (deficit)	$
	===

RATEXCHANGE CORPORATION

(A Development Stage Company)

CONSOLIDATED STATEMENT OF OPERATIONS

	Three Months ended September 30, (unaudited)		Nine Months September (unaudit
	2001	2000	2001
REVENUE			
Trading and consulting	$ 410,439	$ 52,755	$ 1,120,783
EXPENSES			
Selling, general and administrative (includes non-cash expenses of $1,245,000 and $9,974,000 for the three month periods in 2001 and 2000 and $5,423,000 and $21,884,000 for the nine month periods in 2001 and 2000)	3,203,024	16,333,853	15,536,389
Write off advances to potential investee	--	--	--
Depreciation and amortization	562,826	62,983	1,417,623
Purchase of subsidiaries (non-cash)	--	--	--
Write-down of software assets	3,010,371	--	3,010,371
Loss or settlement on leases	7,039,397	--	7,039,397
Total Expenses	13,815,618	16,396,836	27,003,780
OTHER INCOME (EXPENSE)			
Interest income	41,925	392,300	316,205
Interest expense	(22,151)	(1,581,234)	(30,901)
Loss on securities	--	--	(744,197)
Other expenses (net)	(207,107)	(324,375)	(207,107)
Loss before taxes	(13,592,512)	(17,857,390)	(26,548,997)
Income tax provision (benefit)	--	--	--
NET LOSS	$(13,592,512)	$(17,857,390)	$(26,548,997)

Basic and diluted net loss per share	$ (0.76)	$ (1.03)	$ (1.50)
Weighted average number of shares of common stock	17,880,391	17,356,043	17,815,821

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RATEXCHANGE CORPORATION
(A Development Stage Company)
CONSOLIDATED STATEMENT OF CASH FLOWS

	For the nine m ended Septembe 2001 (Unaudited) (restated)
CASH FLOWS FROM OPERATING ACTIVITIES	
Net loss	$(26,548,997)
Adjustments to reconcile net loss to net cash used in operating activities	
Depreciation and amortization	1,417,623
Write off advances to potential investee	
Write-down of software assets	3,010,371
Stock options and warrants granted to service providers and strategic partners	633,831
Stock options granted to employees below fair market value	1,565,694
Stock options - termination adjustment	565,875
Warrants issued in relation to bridge financing	
Warrants for purchase of common stock issued for services	--
Stock Issued for services	145,200
Purchase of outstanding shares of RateXchange	--
Deferred lease payments	1,286,000
Loss or settlement on leases	7,039,397
Deferred compensation	558,109
Loss on writedown of securities	744,197
Increase in security deposits	(10,437)
(Increase) decrease in accounts receivable and other advances	(55,481)
Increase (decrease) in accounts payable and accrued expenses	(1,373,111)
Net cash used in operating activities	(11,021,729)
CASH FLOWS FROM INVESTING ACTIVITIES	

Payment for purchase of equipment	(42,900)
Purchase of Halo Stock	
Purchase of investments available for sale	
Sale of investments available for sale	11,580,361
Investment in Affiliates	(500,000)
Net cash provided by/(used in) investing activities	11,037,461
CASH FLOWS FROM FINANCING ACTIVITIES	
Loans and other debt	--
Proceeds from common stock sales (net)	--
Proceeds from notes receivable	--
Net cash provided by financing activities	--
INCREASE IN CASH AND CASH EQUIVALENTS	15,732
CASH and CASH EQUIVALENTS BEGINNING OF PERIOD	2,115,152
CASH and CASH EQUIVALENTS END OF PERIOD	$ 2,130,884

RATEXCHANGE CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 INTERIM FINANCIAL STATEMENTS, COMPANY BACKGROUND AND HISTORY

The interim financial statements presented herein are unaudited and have been prepared in accordance with the instructions to Form 10-Q. These statements should be read in conjunction with the financial statements and notes thereto included in our annual report on Form 10-K for the year ended December 31, 2000. The results of operations and cash flows for the three and nine months ended September 30, 2001 may not be indicative of the results that may be expected for the year ending December 31, 2001.

RateXchange Corporation (the "Company" or "RateXchange") is a consolidated group of companies including the parent corporation, RateXchange Corporation (RateXchange Corp.), and its subsidiaries, RateXchange I, Inc., Xpit Corporation ("Xpit"), RMG Partners Corporation ("RMG"), and PolarCap, Inc. (PolarCap). PolarCap is in the process of being liquidated.

RateXchange Corporation (formerly NetAmerica.com Corporation) is a Delaware corporation originally organized on May 6, 1987 for the purpose of seeking out and developing any general business opportunity. The Company's operating subsidiary RateXchange I, Inc., a Delaware corporation organized in June 1999, has developed proprietary trading software to support its electronic trading system for bandwidth and other telecommunications products. In March 2001, the Company acquired Xpit.com, Inc., an Idaho corporation offering trading and risk management systems to the futures industry. In October 2001, substantially all of the assets acquired were sold to CQG, Inc. In April 2001, RateXchange formed RMG Partners Corporation, a wholly owned subsidiary, to provide market-based solutions through the use of derivative trading strategies.

RateXchange Corporation is an innovative transaction services firm that combines the strength of traditional voice brokerage with technology-based trading systems to help its clients understand and compete in newly commoditizing marketplaces. RateXchange's mission is to provide an unbiased view and help increase liquidity in these marketplaces by providing brokerage, consulting and information services that enable network providers, energy merchants and financial services firms to maximize the usage of their assets. The brokerage services include traditional voice brokerage, including securities brokerage, in addition to a proprietary trading system, the RateXchange Trading System (RTS), that allows network providers, energy merchants, financial institutions, asset managers and commodity traders the ability to trade bandwidth and bandwidth-related products. The consulting

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solutions practice provides asset valuation tools, risk management strategies and price analysis. The information services include the provision of bandwidth pricing information, market research and comprehensive analysis for industry segments supported by the Company's trading system.

The Company is defined as a development stage company in accordance with Financial Accounting Standard No. 7. The Company began revenue generation activities in 2000 but nominal revenue has been generated through September 30, 2001. The Company anticipates that the revenue growth that has occured, in addition to other factors related to the Company's operations, will result in the removal of the development stage company classification in the fourth quarter of 2001.

In April 2001, as previously disclosed in the year 2000 Form 10K, the Company received an irrevocable commitment from two investors to acquire a total of $9 million of common stock to be issued from capital shares. During the second quarter of 2001, management was informed by those investors that they did not expect to honor the original commitment due to the decline in the Company's share price. As a result of this development, management is seeking a reduced amount of financing in the amount of $2.5 million and in no event more than $3.5 million, that the Company expects to close before the end of November 2001. As of November 20, 2001, the Company had opened escrow into which approximately $2.9 million had been received. Additionally, on October 29, 2001, the Company sold substantially all of the assets related its Xpit Corporation subsidiary for $1.0 million in net cash, in addition to the retirement of a related $500,000 note payable (See Note 11 - Subsequent Events).

In November 2000, new management began to implement cost cuts in order to more closely tie costs to revenue. Significant expense reductions have continued through October 2001, which included, among other things, staff reductions, settlement of outstanding obligations associated with unused equipment and completion of certain development efforts that have significantly reduced expenditures for outside consulting expertise. The Company believes that a successful closing of the current financing will be sufficient to fund operations for the next 12 months. The Company cannot make assurances that it will be able to complete the full financing, or that such financing will be adequate for the Company's needs.

The factors discussed above create substantial doubt about the Company's ability to continue as a going concern and an uncertainty as to the recoverability and classification of recorded asset amounts and the amounts and classification of liabilities. The accompanying financial statements do not include any adjustments relating to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Company be unable to continue as a going concern.

NOTE 2 CASH, CASH EQUIVALENTS AND SHORT TERM INVESTMENTS

We consider all highly liquid investment securities with original maturities of three months or less from date of purchase to be cash equivalents. Short-term investments consist of debt securities with maturities between three months and twelve months.

Management determines the appropriate classification of investments at the time of purchase and reevaluates such determination at each balance sheet date. To date, all marketable securities have been classified as available-for-sale and are carried at fair value with unrealized gains and losses, if any, included in stockholders' equity. At September 30, 2001, the Company had no investments in securities available for sale. Realized gains and losses and declines in value of securities judged to be other than temporary are included in other income, net. Interest and dividends on all securities are included in other income, net.

NOTE 3 SERIES A PREFERRED STOCK

In the first quarter of 2001, in conjunction with the purchase of Xpit.com., the Company issued 2,000,000 shares of

its Series A Convertible Preferred Stock with a cumulative dividend of 6% based on a share price of $2.75 per share. Dividends are paid in shares of Series A Preferred Stock. The Series A Preferred Stock is convertible on a one for one basis into common shares of the Company at the discretion of the holders. The holder of each share of Series A Preferred Stock has the right to one vote for each share of Common Stock into which such share of Series A Preferred Stock could then be converted. In the event of any liquidation, dissolution, or winding up of the Company, whether voluntary or involuntary, the holders of the Series A Preferred Stock are entitled to receive, prior and in preference to any distribution of any assets or surplus funds of the Company to the holders of common stock, the aggregate amount of $2.75 per share (as adjusted for any stock dividend, combinations, or splits with respect to such shares). The Series A preferred stock is not redeemable.

NOTE 4 LOSS PER SHARE AND AVERAGE SHARES OUTSTANDING

Basic loss per share is computed by dividing the net loss, less accrued dividends on preferred stock ($82,500 and $182,000 for the three and nine months ending September 30, 2001), by the weighted average number of common shares outstanding. Options, warrants and convertible preferred stock on shares of common stock were not included in computing diluted loss per share because their effects were anti-dilutive. (10,537,000 options, 6,435,000 warrants and 2,000,000 convertible preferred shares).

NOTE 5 COMMITMENTS AND CONTINGENCIES

The Company is involved in the following lawsuits:

Martin v. RateXchange

On October 3, 2001, Gregory Martin and Patricia Whitney filed a lawsuit against RateXchange Corporation in the United States District Court for the Western District of Washington, C01-1565R alleging breach of contract. In 1998, Mr.

Martin was the President and CEO of NetAmerica International Corporation (NAMI), a predecessor of RateXchange Corporation. In December of 1998 Mr. Martin was terminated from his employment with NAMI. The claims allege breach of agreements associated with Mr. Martin's employment. The complaint asks for damages of approximately $150,000.

Mr. Martin had filed suit previously in the Washington State court. That matter was dismissed following a settlement in May of 1999. Mr. Martin has now revived his claim against the Company.

The Company was recently served with the lawsuit and has not yet responded in court.

YellowBrix, Inc. v. RateXchange Corporation

On October 2, 2001, YellowBrix, Inc. filed a lawsuit against RateXchange Corporation in the Circuit Court for the City of Alexandria, Virginia alleging breach of contract. YellowBrix, Inc. provided news wire information to the Company in 2001. The complaint asks for damages of approximately $32,000. The Company was recently served with the lawsuit and has not yet responded in court.

RateXchange, Inc. v. PWREF/MCC-China Basin, LLC

In September of 2001, RateXchange I, Inc., one of the Company's Delaware subsidiaries, terminated its lease and filed a lawsuit against PWREF/MCC-China Basin, LLC, its previous landlord, alleging constructive eviction and seeking declaratory relief. The allegations of the complaint arise from the lease for commercial space between the parties for the property located at 185 Berry Street, in San Francisco, California. PWREF/MCC-China Basin, LLC has recently responded to the complaint and filed a cross-complaint against RateXchange I, Inc. The Company has reserved $132,000 to address this matter.

Based upon the facts known to the Company at this time and the applicable law, RateXchange does not expect the above cases to result in significant exposure to the Company and the Company has not set aside any additional reserves for the contingencies listed above.

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NOTE 6 COMPREHENSIVE LOSS

The comprehensive loss for the three and nine month periods ending September 30, 2001 and 2000 was:

	Three Months Ended September 30	
	2001	2000
Net loss	$(13,592,512)	$(17,857,390)
Other Comprehensive Income:		
Unrealized losses on short-term investments		(521,513)
Comprehensive loss	$(13,592,512)	$(18,378,903)

NOTE 7 OPERATING LEASES

The Company has entered into various operating leases associated with its delivery hubs, including various telecommunications routing equipment and other infrastructure. In addition, it has entered into various leases for office space and related office equipment, including computers and software. These operating leases have since been settled or restructured, as described below.

Future annual minimum lease payments related to equipment and office space under non-cancelable operating leases as of September 30, 2001 were:

Year	
2001 (Last three months)	$ 393,320
2002	1,936,586
2003	4,895,888
	$7,225,794

During the second quarter, the Company and Forsythe McArthur ("Forsythe") entered into a Restructure Agreement with respect to an equipment lease on delivery hub equipment. The terms of the Restructure Agreement required 12 monthly payments of $74,056 beginning on May 1, 2001, 12 monthly payments of $148,113 beginning on May 1, 2002 followed by one payment on May 1, 2003 of $4,184,544. In September, Forsythe agreed to allow RateXchange to withhold scheduled payments through December 31, 2001, subject to a proposed further restructuring of the lease.

The proposed modified Restructure Agreement between RateXchange and Forsythe is subject to the successful closing of a minimum of $2 million in financing prior to December 31, 2001. The proposed terms call for a $5.95 million five-year convertible note issued to Forsythe, with interest of 9% per annum, payable quarterly in cash or RateXchange common stock. The corresponding leased assets would then be carried on RateXchange's balance sheet. No principal repayments are required prior to the August 31, 2006 maturity date, and the note is convertible at maturity at a 20% discount to the prevailing market price of RateXchange common stock. In consideration for agreeing to modify the Restructure Agreement, Forsythe will receive warrants to purchase $250,000 worth of RateXchange common stock based on a price equal to 130% of the average closing price in October 2001, or $0.48. The warrants will not be exercisable until October 31, 2002. Because the outcome of the financing is not known at this time, the Company's September 30, 2001 financial statements do not reflect the impact of this pending modification to the Restructure Agreement.

As reported in the previous quarters, management has been re-examining its business plans, including aspects of the business related to the delivery hubs and evaluating alternative uses for such leased equipment. During the third quarter, management concluded that it cannot determine a use for such equipment in its ongoing operations. As a

result of the related assets being no longer utilized in the Company's operations, RateXchange took a $6.4 million charge for the acceleration of remaining contractual obligations and costs associated with the Forsythe lease arrangement.

Also during the third quarter, the Company settled claims and additional outstanding lease obligations related to assets and facilities that no longer fit with the revised operating plan. In August 2001, the Company settled its outstanding litigation with Switch and Data Facilities Company. The settlement had a value of $368,000, including a cash payment of $250,000 and Company stock valued at $118,000.

The Company also settled the terms of its collocation lease with Telecity by providing consideration of $275,000 in cash and an agreement to pay $95,000 over six months in return for elimination of all liabilities related to the lease, which totaled approximately $1.2 million.

Additionally, the Company agreed to settle an obligation to Science Applications International Corp. ("SAIC") for goods and services associated with delivery hub equipment. Currently, there is an amount payable to SAIC of approximately $158,000, with $50,000 payable in cash and the balance payable in 175,000 shares of restricted RateXchange common stock.

The Company has an existing lease with Lawson Software for accounting software that it no longer utilizes. The Company has suspended lease payments since September 2001, when negotiations began regarding a concession. An outstanding obligation of $263,000 remains on the lease, and has been fully expensed.

On October 5, 2001 RateXchange signed an 18-month sub-lease for new office space at 100 Pine Street in San Francisco's financial district. Monthly payments are approximately $7,800.

NOTE 8 AGREEMENT WITH AMEREX BANDWIDTH

In September 2001, the Company and Amerex extended their agreement through December 31, 2001. Under the new terms of the extended agreement, the Company maintains its receipt of 70% on all bandwidth brokerage commission revenue generated, and decreases its payment of monthly expenses associated with this revenue from approximately $70,000 per month to $15,000 per month for the remainder of the year.

In July 2001, RateXchange agreed to preliminary non-binding terms for the purchase of all of the outstanding stock of Amerex Bandwidth, Ltd., subject to the signing of a Definitive Agreement and the successful completion of a minimum of $3 million in financing. The transaction was structured as a stock-for-stock purchase, with a portion of the purchase price payable in stock upon the achievement of certain revenue targets. Assuming a successful closing, Amerex Bandwidth would operate as a wholly-owned subsidiary of RateXchange and would remain in its Houston offices. Once RateXchange's current financing is completed, the Company will continue to explore mutually agreeable terms for the acquisition of Amerex Bandwidth. Should the stock purchase not occur, the Company expects to continue its partnership agreement under mutually agreeable terms. Because the future terms of our agreement with Amerex are not known at this time, the Company's September 30, 2001 financial statements do not reflect the impact of this potential acquisition.

NOTE 9 RMG PARTNERS

In April 2001, the Company formed RMG Partners Corporation (RMG) as a wholly owned subsidiary created to provide market-based solutions through the use of derivative trading strategies. RMG principals receive 85% of revenues, which is used to cover payroll and all of the operating expenses of RMG. In connection with his hiring, the CEO of RMG has been given the right to acquire a specific number of shares of the Company with additional purchase rights upon achievement of revenue targets in the future. This deferred compensation is reflected as a component of equity in the balance sheet and is being amortized over a period of 12 months. The Company has granted an affiliate of the principals of RMG the right to purchase RMG for $300,000 commencing in April 2002.

NOTE 10 NEW ACCOUNTING STANDARD

In the first quarter of 2001, the Company was required to adopt the provisions of Financial Accounting Standard Statement No. 133, Accounting for Derivative Instruments and Hedging Activities (FAS 133) as amended by FAS

137 and FAS 138. This statement establishes accounting and reporting standards for derivative contracts and for hedging activities. As the Company does not currently use any derivative instruments or engage in hedging activities, adoption of this new standard had no impact on the Company's consolidated results of operations or consolidated financial position.

NOTE 11 SUBSEQUENT EVENTS

Sale of Xpit Corporation Assets to CQG, Inc.

On October 29, 2001 the Company sold all of the material assets of the Company's Xpit Corporation subsidiary, including the RateXchange Futures System ("RFS"), to CQG, Inc. ("CQG"), a privately-held quotation services company. The assets were sold to CQG in exchange for $1.5 million in cash. Additionally, the Company can earn royalties of up to $650,000 over the next four years if CQG achieves future revenue targets via the RFS platform.

In view of the sale to CQG, the Company recorded a $3.0 million non-cash charge in the third quarter to reflect the impairment in the value of the Xpit Corporation assets, principally the carrying value of the RFS platform. Additionally, the $500,000 note payable associated with the original Xpit purchase price, payable to affiliates of two of RateXchange's Directors, was paid in full, plus accrued interest. Net cash proceeds to the Company, after payment of the note and expenses associated with the transaction, were $902,000.

Private Placement of $2.5 million Convertible Subordinated Notes

As of November 20, 2001, the Company was in the process of raising $2.5 million, and in no event more than $3.5 million, in a private placement financing, which the Company expects will close before the end of November. The offering consists of 50 units, with each unit consisting of a ten-year $50,000 12% convertible subordinated note and warrants to acquire 12,500 shares of RateXchange common stock. The conversion price of the note and the exercise price of the warrants will be the greater of $0.35 or the closing price of RateXchange common stock as evidenced by the last trade on the AMEX prior to the closing of the sale of the units. The warrants will be exercisable for three years following the closing.

The offering is on a best efforts basis, with current funds raised being held in an escrow account. However, upon closing, all funds raised, less the expenses of the offering, will be made available for use by the Company. No assurances can be made that the Company will complete the full funding. As of November 20, 2001, approximately $2.9 million had been received in the escrow account.

Establishment of a Broker/Dealer Operation

RateXchange plans to supplement its transaction services business with a traditional broker/dealer operation focused on the trading and brokerage of stocks, bonds and derivatives thereof. Management believes the current retrenchment and consolidation in the brokerage business provides the opportunity to capitalize on the availability of high quality employees. Given the volatility of the market for telecom debt and equity securities, RateXchange has seen considerable interest in bandwidth pricing and other telecom related data from institutional fund managers. RateXchange owns a NASD approved broker/dealer, has entered into an initial clearing agreement with a bulge bracket clearing firm, and has begun its recruiting process. The Company anticipates beginning NASD fully approved brokerage operations in January of 2002.

NOTE 12 RELATED PARTY REVENUE

In October 2001, the Company successfully completed the process of obtaining a broker/dealer license for its subsidiary, RMG Partners Corporation. With this approval, the Company can continue to pursue its various consulting and risk management services. Prior to obtaining this separate license, the Company completed certain of its consulting and risk management transactions through a registered broker/dealer in which certain Company personnel have a financial interest.

Item 2 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with our Consolidated Financial Statements and the notes thereto presented in "Item 1 - Financial Statements." The information set forth in this "Management's Discussion and Analysis of Financial Condition and Results of Operations" includes forward-looking statements that involve risks and uncertainties. Many factors could cause actual results to differ materially from those contained in the forward-looking statements below. See "Outlook."

The Company is defined as a development stage company in accordance with Financial Accounting Standard No. 7. The Company began revenue generation activities in 2000 but nominal revenue has been generated through September 30, 2001. The Company anticipates that the revenue growth that has occurred, in addition to other factors related to the Company's operations, will result in the removal of the development stage company classification in the fourth quarter of 2001.

GENERAL DEVELOPMENT OF BUSINESS

RateXchange Corporation is an innovative transaction services firm that combines the strength of traditional voice brokerage with technology-based trading systems to help its clients understand and compete in newly commoditizing marketplaces. RateXchange's mission is to provide an unbiased view and help increase liquidity in these marketplaces by providing the following services that enable network providers, energy merchants and financial services firms to maximize the usage of their assets:

- Brokerage Services - These services include traditional voice brokerage, including securities brokerage, in addition to a proprietary trading system, the RateXchange Trading System (RTS), that allows network providers, energy merchants, financial institutions, asset managers and commodity traders engaged on the RTS the ability to trade bandwidth and bandwidth-related products.

- Consulting Solutions - The consulting solutions practice provides asset valuation tools, risk management strategies and price analysis.

- Information Services - These services include the provision of bandwidth pricing information, market research and comprehensive analysis for industry segments supported by the Company's trading system.

RateXchange plans to supplement its transaction services business with a traditional broker/dealer operation focused on the trading and brokerage of stocks, bonds and derivatives thereof. Management believes the current retrenchment and consolidation in the brokerage business provides the opportunity to capitalize on the availability of high quality employees. Jon Merriman, Chairman and CEO of RateXchange, has significant depth of experience in the brokerage business. Merriman's representative background includes: management of Wells Fargo Van Kasper's Capital Markets area, where he oversaw research, sales, trading, derivatives and syndicate; formation of an equity brokerage and investment banking operation at Dabney/Resnick/Imperial LLC, which was subsequently acquired by Imperial Credit Industries; management of the equity market neutral hedge fund Merriman Capital Management Inc; and employment as a risk arbitrage trader and investment banker at Bear, Stearns and Merrill Lynch & Co., respectively.

Given the volatility of the market for telecom debt and equity securities, RateXchange has seen considerable interest in bandwidth pricing and other telecom related data from institutional fund managers. Senior management of RateXchange, as well as the company's Board of Directors, has considerable experience and contacts in the securities business and believes there is an opportunity to drive bandwidth information revenues through a traditional NASD broker/dealer structure. RateXchange owns a NASD approved broker/dealer, has entered into an initial clearing agreement with a bulge bracket clearing firm, and has begun its recruiting process. The company anticipates beginning NASD fully approved brokerage operations in January of 2002.

On August 18, 2001, RateXchange entered into an agreement with Reuters Group PLC, a major financial news organization with over 600,000 subscribers worldwide, to offer real-time bandwidth pricing information and market commentary. The companies expect to formally and jointly announce the agreement in the fourth quarter of 2001, after the completion of beta testing and successful deployment of the service. The Company expects that this arrangement, if successful, will strengthen RateXchange's branding as a recognized leader in bandwidth pricing information.

On August 14, 2001, RateXchange and Dorado Software announced a strategic agreement to automate Internet Protocol or "IP" service delivery in the bandwidth trading marketplace. Dorado's software can reserve, deliver and monitor services in the bandwidth trading market, overcoming many of the challenges of managing the delivery of IP services.

On July 31, 2001, RateXchange announced that it had completed development of its new Metro Bandwidth Trading Service designed to allow customers to buy and sell metro bandwidth capacity. This new product is a solution for trading metro capacity and helps break down the local loop bottleneck that currently exists. This trading solution was developed in close cooperation with several optical metropolitan-area network providers. The Metro Bandwidth Trading Service was designed to accommodate the needs of both these new metro providers, as well as being available for use by the incumbent providers. The service is expected to facilitate overall bandwidth trading by addressing a critical area in today's market - connectivity at the local level.

On July 16, 2001, RateXchange announced an agreement with Avantrust, LLC, a joint venture between American International Group, Inc. (NYSE:AIG) and Dun & Bradstreet (NYSE:DNB), whereby Avantrust Passport and TradeCredit Insurance will be provided to participants on all RateXchange telecom markets. As a result, all RateXchange buyers will have their credit information available to do business, and all qualified sellers will be able to arrange for trade credit insurance to cover against buyer non-payment. This product offering provides a unique value proposition to RateXchange's sellers, who will have insured payments on approved parties, as well as RateXchange's buyers, who can avoid cash deposits or letters of credit. The Company expects this product offering to be available for all RTS bandwidth markets including TDM bandwidth and IP trading products.

Results of Operations for Three and Nine Months Ended September 30, 2001

The following table summarizes our results of operations for the three and nine month periods ending September 30, 2001, compared to the same periods of 2000.

	Three Months Ended September 30	
	2001	2000 (restated)
Revenue	$ 410,439	$ 52,755
Recurring Operating Expenses	$ 3,765,850	$ 16,396,836
Non-Recurring Operating Expenses	$ 10,049,768	--
Net income (loss)	$(13,592,512)	$(17,857,390)

Third quarter results:

Revenue

The Company generated revenue of $410,439 for the three-month period ending September 30, 2001. Revenue in this period was primarily from consulting fees, and to a lesser extent trading commissions. In the comparable period of 2000, the Company generated revenue of $52,755, primarily from consulting fees.

Recurring Operating Expenses

Total recurring operating expenses for the third quarter ending September 30, 2001 were $3.8 million compared to $16.4 million for the third quarter of 2000, reflecting an improvement of 77% year-over-year. The decrease in recurring operating expenses was primarily a result of staff reductions, a significant decrease in option and warrant expense related to employees and service providers, and the elimination of expenses not directly tied to revenue growth.

Total recurring cash operating expenses decreased 69% to $2.0 million compared to $6.4 million for the third quarter of 2000. The decrease was a result of staff reductions, cost reductions associated with the completion of systems development efforts, and the elimination of delivery equipment costs. The major components of our recurring cash expenses for the third quarter of 2001 were:

Recurring Cash Expenses

- $925,000 in payroll costs during the third quarter of 2001 compared to $1,910,000 in the third quarter of 2000;

- $309,000 in outside services during the third quarter of 2001 compared to $725,000 during the third quarter of 2000, and;

- $222,000 in delivery equipment costs for the third quarter of 2001 compared to $1,719,000 in the third quarter of 2000 (excluding the acceleration of $6.4 million of remaining lease commitments as described below).

Total recurring non-cash operating expenses for the third quarter decreased 82% to $1.8 million compared to $10.0 million for third quarter of 2000. This decrease was primarily due to the significant decrease in option expense related to service providers and employees no longer with the Company. The major components of our non-cash expenses for the third quarter of 2001 were:

Recurring Non-Cash Expenses

- $643,000 related to amortization of deferred lease payments. There were no such expenses in the same period of 2000

- $363,000 compared to $1,484,000 in the third quarter of 2000 for amortization expense associated with the year 2000 grant of below market stock options to employees;

- $563,000 compared to $63,000 for the third quarter of 2000 for depreciation expense;

- $93,000 compared to $8,095,000 for the third quarter of 2000 for options and warrants to service providers

Non-Recurring Operating Expenses

Other non-recurring operating expenses for the third quarter amounted to approximately $10.1 million compared to none in the third quarter of 2000. During the quarter, the Company recognized the acceleration of $7.0 million in lease obligations, settlements and costs associated with equipment and facilities no longer in use, in addition to a $3.0 million write-down of Xpit Corporation assets subsequently sold to CQG, Inc., principally the carrying value of the RFS platform. Of these non-recurring charges, $9.5 million were non-cash. $5.3 million of these charges are related to the Forsythe lease, are currently due in May 2003 and will be rescheduled for payment in August 2006 upon successful completion of the Company's current funding round.

Interest Income/Expense:

Interest income for the third quarter of 2001 was $42,000 compared to $392,000 for the third quarter in 2000. The decrease in interest income is due to less interest earned on a smaller average investment portfolio. Interest expense of $22,000 for the third quarter was attributable to the $500,000 note payable, which was subsequently repaid during the fourth quarter upon the sale of the Xpit Corporation assets.

Other Expenses

Other non-recurring expenses for the third quarter amounted to approximately $207,000 compared to $325,000 in the third quarter of 2000, due to cost cutting measures enacted by the Company during the third quarter of 2001.

Net Loss:

During the third quarter of 2001, the Company incurred a loss of $13.6 million compared to $17.9 million during the third quarter of 2000. The major components of the net loss for the third quarter were $7.0 million in non-recurring charges associated with leased assets no longer in use, a $3.0 million write-down on the value of the Xpit Corporation assets, and additional cash expenditures of $2.0 million associated with operating the business. These cash expenditures were down from $2.5 million in the second quarter of 2001, representing a 20% quarter-over-quarter improvement.

Due to the recognition of one-time charges associated with unused equipment and facilities and the write-down of the Xpit assets, the Company expects future results to more directly reflect current operations.

Nine-month results:

Revenue

The Company generated revenue of $1,121,000 for the nine-month period ending September 30, 2001, primarily from consulting fees, and to a lesser extent trading commissions. In the comparable period of 2000, the Company generated $57,000, primarily from consulting fees.

Recurring Operating Expenses

Total recurring operating expenses for the nine-months ending September 30, 2001 were $17.0 million compared to $36.1 for the same period in 2000, reflecting a decrease of 53%. This decrease was primarily due to the significant decrease in option expense related to service providers and employees no longer with the Company during 2001.

Total recurring cash operating expenses for the nine-month period decreased 29% to $10.1 million compared to $14.2 for the same period in 2000. The decrease was a result of cost reductions associated with the completion of systems development efforts, staff reductions, and the elimination of expenses not directly tied to revenue growth. The major components of our cash expenses for the nine-month period ending September 30, 2001 were:

Recurring Cash Expenses

- o $3,247,000 in payroll costs during the nine-month period compared to $3,880,000 during the same period of 2000;
- o $2,084,000 in outside services compared to $2,584,000 during the same period in 2000, and;
- o $2,436,000 for delivery equipment costs compared to $2,454,000 in the same period in 2000.

Total recurring non-cash operating expenses for the nine-month period ending September 30, 2001 decreased 69% to $6.8 million from $22.0 million for 2000, primarily due to the significant decrease in option expense related to service providers and employees no longer with the Company. The major components of our recurring non-cash expenses for the nine-month period ending September 30, 2001 were:

Recurring Non-cash Expenses

- $1,566,000 compared to $9,128,000 for the same period in 2000 for amortization expense associated with the year 2000 grant of below market stock options to employees;

- $1,418,000 compared to $164,000 for the same period in 2000 for depreciation expense;

- $558,000 for deferred and accrued compensation. There were no such expenses in the similar period of 2000;

- $633,000 for option revaluation related to terminated employees. There were no such expenses in the similar period of 2000;

- $379,000 compared to $11,711,000 in the same period of 2000 for options and warrants granted to service providers;

- $1,286,000 related to amortization of deferred lease payments. There were no such expenses in the same period of 2000.

- $577,000 of accruals related to contingent liabilities. The comparable amount in the 2000 period was $250,000.

Non-Recurring Operating Expenses

Other non-recurring operating expenses for the nine-month period ending September 30, 2001 amounted to approximately $10.1 million compared to none in the similar period of 2000. During the third quarter of 2001, the Company recognized the acceleration of $7.0 million in lease obligations, settlements and costs associated with equipment and facilities no longer in use, in addition to a $3.0 write-down of Xpit Corporation assets subsequently sold to CQG, Inc. Of these non-recurring charges in the third quarter, $9.5 million were non-cash. $5.3 million of these charges are related to the Forsythe lease, are currently due in May 2003 and will likely be rescheduled for payment in August 2006 upon completion of the Company's current funding round.

Interest Income/Expense:

Interest income for the first nine months of 2001 was $316,000 compared to $605,000 for the same period in 2000. The decrease in interest income is due to less interest earned on a smaller average investment portfolio. Interest expense of $31,000 for the nine-month period was primarily attributable to the $500,000 note payable, which was subsequently repaid during the fourth quarter upon the sale of the Xpit Corporation assets.

Other Expenses:

Other non-recurring expenses for the nine-month period ending September 30, 2001 amounted to approximately $1.0 million compared to $1.8 million in the similar period of 2000. During the first two quarters of 2001, the Company recognized a loss on sale of securities held of $0.7 million.

Net Loss:

During the nine-month period ending September 30, 2001, the Company incurred a loss of $26.6 million compared to $39.1 million during the same period of 2000. The major components of the net loss for the recent nine-month period were $7.1 million in non-recurring charges associated with leased assets, a $3.0 million write-down on the value of the Xpit Corporation assets, and additional cash expenditures of $10.1 million associated with operating the business.

LIQUIDITY AND CAPITAL RESOURCES

RateXchange has financed its operations to date primarily through the sale of equity securities. The Company has been unprofitable since inception and has incurred net losses in each year.

Cash and cash equivalents at September 30, 2001 were $2.1 million compared to $4.9 million on June 30, 2001 and $14.2 million on December 31, 2000.

As previously disclosed in the year 2000 Form 10K, in April 2001, the Company received an irrevocable commitment from two investors to acquire a total of $9 million of newly issued common shares of the Company. During the second quarter of 2001, management was informed by those investors that they did not expect to honor the original commitment due to the decline in the Company's share price. As a result of this development, in addition to the expense reductions undertaken by the Company, management is in the process of raising $2.5 million, and in no event more than $3.5 million, in a private placement of convertible subordinated notes, which it expects to close before the end of November. As of November 20, 2001, the Company has opened escrow into which approximately $2.9 million has been received. Management expects that this financing will be sufficient to fund its operations for at least the next twelve months (See Note 11 - Subsequent Events).

In the fourth quarter of 2000, new management began to implement cost cuts in order to more closely tie costs to revenue. Significant expense reductions have continued through October 2001, which included, among other things, the sale of the Xpit assets, staff reductions, elimination of obligations related to leased equipment and facilities, and the elimination of nearly all outside consulting services. Although the Company expects its current financing will be sufficient to meet its needs, it cannot make assurances that it will be able to raise the total amount, or that such amount will be adequate for the Company's needs.

The factors discussed above create substantial doubt about the Company's ability to continue as a going concern and an uncertainty as to the recoverability and classification of recorded asset amounts and the amounts and classification of liabilities. The accompanying financial statements do not include any adjustments relating to the recoverability and classification of asset carrying amounts or the amount and classification of liabilities that might result should the Company be unable to continue as a going concern.

The Company has continued to lower its operating costs, including a reduction in its workforce, a further reduction in management salaries and the elimination of additional operating expenses, including all consulting expenses. Management is working aggressively on these factors to ensure that it is fully able to execute on its current business plan. We have taken the following steps to achieve profitability:

- We completed the sale of the Xpit assets to CQG help strengthen the Company's balance sheet, reduce the monthly cash burn, and allow the Company to focus on its core businesses of brokerage, consulting and information services.

- We are pursuing additional revenue generating opportunities such as the establishment of a securities broker/dealer that may accelerate our development of a financial services business model;

- We have re-negotiated or settled existing claims and obligations with respect to unused equipment and space at a discount to the value of the associated liabilities;

- Upon the successful completion of our current financing above a minimum of $2 million, we will effect a restructuring of our agreement with respect to the operating lease underlying our delivery equipment, resulting in the creation of a $5.95 million five-year 9% convertible note, with interest payable in cash

or Ratexchange common stock. This will reduce our cash expense associated with this lease from $74,000 per month through April 2002 and $148,000 per month through April 2003, to approximately $44,000 per month through August 2006, and will extend an increased balloon payment from $4.2 million to $5.95 million out an additional 39 months to August 2006;

- We have reduced our number of employees and associated personnel costs; our employee headcount in our San Francisco location has been reduced from 37 at December 31, 2000 to 11 currently. Including the five employees at our subsidiary RMG Partners, there are a total of 16 employees; and

- We have significantly reduced our marketing and public relations costs.

Net cash used in operating activities was $11.0 million for the nine months ending September 30, 2001, compared to $13.8 million for the comparable period in 2000. Net cash used in operating activities during the first nine months of 2001 was due primarily to:

- Costs associated with accelerating the deployment of the RateXchange Trading System;

- Ongoing business development activities;

- Settlement of claims and lease obligations related to unused equipment and space.

Net Cash provided by investing activities was $11.0 million for the first nine months of 2001, due primarily to the sale of marketable securities.

We are executing an overall business plan that will require additional capital for, among other uses:

- Funding operating losses and ongoing working capital needs;
- Development of additional products and services, such as IP and Metro Trading products;
- Support of the operating expenses of Amerex Bandwidth; and
- Development and growth of a securities broker/dealer

We currently anticipate that our available funds, consisting of cash, cash equivalents and investments, combined with those funds raised through the sale of the Xpit assets and the anticipated net proceeds from our current financing, will be sufficient to meet our anticipated needs for working capital and capital expenditures through at least the next 12 months. Our future long-term capital needs will depend significantly on the rate of growth of our business, the timing of expanded service offerings, the success of these services once they are launched and our ability to adjust our operating expenses to an appropriate level if the growth rate of our business is slower than expected. Any projections of future long-term cash needs and cash flows are subject to substantial uncertainty. If our available funds and cash generated from operations are insufficient to satisfy our long-term liquidity requirements, we may seek to sell additional equity or debt securities, obtain additional lines of credit, curtail expansion of our services or potentially liquidate selected assets. If we issue additional securities to raise funds, those securities may have rights, preferences or privileges senior to those of the rights of our common stock and our stockholders may experience dilution. We cannot be certain that additional financing will be available to us on favorable terms when required, or at all.

Our business and operations have not been materially affected by inflation during the periods for which financial information is presented.

OUTLOOK

RateXchange is a transaction services firm that combines the strengths of traditional voice brokerage and technology-based trading systems to help its clients understand and compete in newly commoditizing industries. As

a neutral entity that acts as agent rather than taking positions, the Company provides a window to evolving commodity marketplaces by providing information and consulting, similar to the securities industry. The Company also provides a neutral trading system, which offers buyers and sellers the dual benefits of price discovery and anonymity. Customers of RateXchange who are interested in trading bandwidth, such as telecommunications firms, energy merchants and financial services companies, seek in-depth, unbiased market information and pricing on bandwidth, as well as a trusted system to execute their trades. The Company's information services group provides pricing data, supported with market research and comprehensive analysis for industry segments supported by RateXchange's trading systems. The Company's consulting services practice provides asset valuation tools, risk management strategies and price analytics. This combination of RateXchange services helps create liquidity in the marketplace - generating increased trading activity and price information that the Company reflects back into the market.

We plan to move into the brokering of additional products that fit into the brokerage, consulting and information services model. We are pursuing the formation of a securities broker-dealership that may accelerate our development of a financial services business model.

We are a development stage company and we are subject to all the risks inherent in the establishment of a new business enterprise. To address these risks, we must:

- Establish market acceptance for our electronic trading system and other products and services;
- Continue to retain, attract and motivate qualified personnel;
- Effectively manage our capital to support the expenses of developing and marketing new products and services;
- Implement and successfully execute our business and marketing strategy; and
- Respond to competitive developments and market conditions in the global communications industry.

The foregoing contains forward-looking statements that involve risks and uncertainties, including but not limited to changes in our business strategy, our inability to raise sufficient capital, general market trends and conditions, and other risks detailed below in "Factors That May Affect Future Results." Actual results may vary materially from any future results expressed or implied by the forward-looking statements.

Forward-Looking Statements

This Outlook section, and other sections of this document, include certain "forward-looking statements" within the meaning of that term in Section 27A of the Securities Act of 1933, and Section 21E of the Securities Act of 1934, including, among others, those statements preceded by, following or including the words "believe," "expect," "intend," "anticipate" or similar expressions. These forward-looking statements are based largely on our current expectations and are subject to a number of risks and uncertainties. Our actual results could differ materially from these forward-looking statements. Important factors to consider in evaluating such forward-looking statements include:

- Changes in our business strategy or an inability to execute our strategy due to unanticipated changes in the market;
- Our ability to raise sufficient capital to meet operating requirements;
- Various competitive factors that may prevent us from competing successfully in the marketplace;
- Changes in external competitive market factors or in our internal budgeting process which might impact trends in our results of operations, and
- Other risks described below in "Factors That May Affect Future Results."

In light of these risks and uncertainties, there can be no assurance that the events contemplated by the forward-looking statements contained in this Form 10-Q will in fact occur.

FACTORS THAT MAY AFFECT FUTURE RESULTS

We operate in a highly competitive and rapidly changing market that involves a number of risks. While we are optimistic about our long-term prospects, the following discussion highlights some risks and uncertainties that should be considered in evaluating our growth outlook.

We will need additional capital in the future and it may not be available on acceptable terms.

As previously discussed, we will need additional funds for enhancement of the IP and Metro Trading products, support of the operations of Amerex Bandwidth, general and administrative costs and to fund losses before achieving profitability. We will need to raise additional funds through additional equity and/or debt financing to meet our capital requirements. We cannot assure you that such financings will be available in amounts or on terms needed to meet our requirements, or at all. Further, our lack of tangible assets to pledge could prevent us from establishing a source of financing. The inability to raise all needed funding would adversely affect our ability to successfully implement the objectives of our business plan.

As a development stage company with a limited operating history in a new and rapidly changing industry, it is difficult to evaluate our business and prospects.

We are a development stage company. Our activities to date have concentrated primarily on planning and developing our electronic trading system for trading bandwidth and other telecommunications products. In September 2000, we began operating the RateXchange Trading System for trading bandwidth. Accordingly, we have a limited operating history on which to base an evaluation of our business and prospects. Our prospects must be considered in light of the risks, expenses and difficulties frequently encountered by companies in their early stage of development, particularly companies in new and rapidly evolving markets such as online commerce. There can be no assurance that we will be successful in addressing these risks and our failure to do so could have a material adverse effect on our business and results of operations.

We have a history of losses and expect to incur losses in the future, and we may never achieve profitability.

At September 30, 2001, our accumulated deficit since inception was $84,051,914, including $39,823,000 related to stock grants, options and warrants. For the third quarter of 2001, we incurred a net loss of $13,592,512, consisting of $7,039,000 in non-recurring charges associated with unused lease equipment and facilities, including warrant and stock option charges, and a $3,010,000 write-down of the Xpit assets. We have incurred a net loss in each year of our existence, and have financed our development stage operations primarily through sales of equity securities. We have recorded nominal revenues from operations. We expect to incur net losses for the foreseeable future. We may never achieve or sustain significant revenues or profitability on a quarterly or annual basis.

If the RateXchange Trading System does not achieve commercial acceptance, our results will suffer.

We expect to rely largely on fees and commissions from transactions facilitated on the RateXchange Trading System and related consulting services for the foreseeable future. Online trading of telecommunications bandwidth currently has only limited market acceptance. As a result, our future ability to gain commercial acceptance of the RateXchange Trading System is critical to our success. Any failure to successfully gain commercial acceptance of the RateXchange Trading System would not only have a material adverse effect on our business and operating results, but also on our ability to seek additional revenue opportunities.

We depend on the efforts of the Amerex Bandwidth, Ltd. brokers who execute trades with the assistance of our trading system to generate revenues for us.

In September 2000, we entered into a strategic alliance with Amerex Bandwidth, Ltd., a leading energy and power broker. Under our agreement with Amerex, Amerex brokers execute trades for the sale or purchase of

telecommunications capacity, Internet protocol products and/or other telecommunications-related products with the assistance of our trading system, and we share with Amerex the revenues generated by these trades. As a result, we depend on the efforts of the Amerex brokers who execute those trades to generate revenues for us. There can be no assurance that these brokers will be successful in expanding our business.

Our agreement with Amerex, which terminates at the end of 2001, currently obligates us to pay for a portion of Amerex's operating expenses. Our failure to renew this agreement on terms acceptable to us could adversely affect our business.

Pursuant to our agreement with Amerex, although we receive 70% of any commissions generated by voice brokerage sales effected by Amerex, we are currently obligated to pay up to $15,000 monthly, reduced recently by amendment from $70,000, to cover Amerex's negative operating expenses. Current monthly brokerage commissions approximate $20,000. Based on current bandwidth trading activity, we estimate that Amerex's negative cash flow from these operations approximates $50,000 per month. Our agreement with Amerex terminates at the end of 2001. We cannot assure that we will be able to extend this agreement on terms acceptable to us, if at all, or if we do that our monthly obligation to pay for Amerex's negative operating expenses will not increase substantially. Our failure to extend this agreement, or, in the alternative, internally develop or otherwise acquire an adequate bandwidth voice brokerage operation would adversely affect our business.

We may not be able to compete successfully against current and future competitors.

The market for the brokerage of bandwidth and related commodities, both regulated and unregulated, is new, rapidly evolving and highly competitive. We expect competition in this market to intensify in the future. Several of the existing online exchanges and brokers, such as E-Speed, Intercontinental Exchange and Altra currently operate online marketplaces in commodities and have large established customer bases. These companies may start bandwidth trading marketplaces. Our ability to compete with them will depend largely upon our ability to capture market share.

In addition, we compete with companies who trade, broker or otherwise assist in the buying and selling of telecommunications bandwidth. Therefore, we currently or potentially compete with a variety of other companies, including lead-generation services and traditional offline brokers. Many companies, such as Band-X, and Arbinet, offer services to buyers and sellers of bandwidth and other telecommunications products. The increased use and acceptance of any other method of facilitating the buying and selling of excess telecommunications bandwidth may adversely impact the commercial viability of the RateXchange Trading System.

Large telecommunications and energy companies have the ability and resources to compete in the online bandwidth trading services market if they choose to do so, including launching their own online exchanges or other trading services. Many of our competitors have substantially greater financial, technical and marketing resources, larger customer bases, longer operating histories, greater name recognition and more established relationships in the industry than we have. In addition, a number of these competitors may combine or form strategic partnerships. As a result, our competitors may be able to offer, or bring to market earlier, products and services that are superior to our own in terms of features, quality, pricing or other factors. Our failure to compete successfully with any of these companies could have a material adverse effect on our business and results of operations.

Increased pressure created by any present or future competitors, or by our competitors collectively, could have a material adverse effect on our business and operating results. Increased competition may result in reduced commissions and loss of market share. Further, as a strategic response to changes in the competitive environment, we may from time to time make certain pricing, service or marketing decisions or acquisitions that could have a material adverse effect on our business and operating results. There can be no assurance that we will be able to compete successfully against current and future competitors. In addition, new technologies and the expansion of existing technologies may increase the competitive pressures on us.

We face online commerce security risks.

We rely on encryption and authentication technology licensed from third parties to provide the security and authentication necessary to effect secure transmission of confidential information, such as bank account or credit information. There can be no assurance that advances in computer capabilities, new discoveries in the field of cryptography, or other events or developments will not result in a compromise or breach of the algorithms used by us to protect transaction data. Any compromise of our security could have a material adverse effect on our reputation and us. A party who is able to circumvent our security measures could misappropriate proprietary information or cause interruptions in our operations. We may be required to expend significant capital and other resources to protect against such security breaches or to alleviate problems caused by such breaches. To the extent that our activities or those of third party contractors involve the storage and transmission of proprietary information, such as bank account or credit information, security breaches could damage our reputation and expose us to a risk of loss or litigation and possible liability which could have a material adverse effect on our business and results of operations.

We may be adversely affected by government regulations and legal uncertainties associated with the Internet.

Laws and regulations directly applicable to Internet communications, commerce and advertising are becoming more prevalent, but the legislative and regulatory treatment of the Internet remains largely unsettled. The U.S. Congress has adopted Internet laws regarding copyright, taxation and the protection of children. In addition, a number of other legislative and regulatory proposals under consideration by federal, state, local and foreign governments could lead to additional laws and regulations affecting, among other things:

- the right to collect and use personally identifiable information;
- pricing;
- intellectual property;
- online content;
- user privacy;
- taxation;
- access charges;
- distribution;
- liability for third-party activities; and
- characteristics and quality of products and services.

For example, the growth and development of the market for Internet commerce may prompt calls for more stringent consumer protection laws in the United States that may impose additional burdens on companies conducting business over the Internet.

The adoption of any additional laws or regulations may decrease the growth of the Internet or other online services, which could, in turn, reduce the demand for our products and services and increase our cost of doing business, or otherwise have an adverse effect on our business and results of operations. Moreover, courts may seek to apply existing laws not explicitly relating to the Internet in ways that could impact the Internet, and it may take years to determine whether and how laws such as those governing intellectual property, privacy, libel and taxation will affect the Internet and our use of it.

We plan to facilitate transactions between numerous customers residing in various states and foreign countries, and such jurisdictions may claim that we are required to qualify to do business as a foreign corporation in each such state and foreign country. Our failure to qualify as a foreign corporation in a jurisdiction where it is required to do so could subject us to taxes and penalties. Any new legislation or regulation, the application of laws and regulations from jurisdictions whose laws do not currently apply to our business, or the application of existing laws and regulations to the Internet and other online services could have a material adverse effect on our business and results of operations.

We have registered our subsidiary RMG as a securities broker/dealer and, as such, are subject to substantial regulations. Our failure to comply with these regulations would adversely affect our business.

We have registered our wholly owned subsidiary RMG Partners Corp. with the SEC as a securities broker/dealer,

and as a result are subject to extensive regulation under federal and state laws. The principal purpose of regulation and discipline of broker/dealers is the protection of customers and the securities markets rather than protection of creditors and stockholders of broker/dealers. The SEC is the federal agency charged with administration of the federal securities laws. Much of the regulation of broker/dealers, however, has been delegated to self-regulatory organizations, such as the National Association of Securities Dealers, Inc. ("NASD"), and national securities exchanges. The NASD is our primary self-regulatory organization. These self-regulatory organizations adopt rules (which are subject to approval by the SEC) that govern the industry and conduct periodic examinations of member broker/dealers. Broker-dealers are also subject to regulation by state securities commissions in the states in which they are registered. The regulations to which broker/dealers are subject cover all aspects of the securities business, including net capital requirements, sales methods, trading practices among broker/dealers, capital structure of securities firms, record keeping and the conduct of directors, officers and employees. The SEC and the self-regulatory bodies may conduct administrative proceedings, which can result in censure, fine, suspension or expulsion of a broker/dealer, its officers or employees. If we fail to comply with these rules and regulations, our business would be materially and adversely affected.

We may face liability for information retrieved from our web site.

Due to the fact that material may be downloaded from our web site and subsequently distributed to others, there is a potential that claims may be made against us for negligence, copyright or trademark infringement or other theories based on the nature and content of such material. Although we carry general liability insurance, our insurance may not cover potential claims of this type or may not be adequate to cover all costs incurred in defense of potential claims or to indemnify us for all liability that may be imposed. Any costs or imposition of liability that is not covered by insurance or in excess of insurance coverage could have a material adverse effect on our business and results of operations.

We are at risk of capacity constraints and face system development risks.

There may be a significant need to upgrade the capacity of the RateXchange Trading System in order to handle thousands of simultaneous users and transactions. Our inability to add additional software and hardware or to develop and upgrade further our existing technology, transaction processing systems or physical infrastructure to accommodate increased traffic on these systems or increased trading volume through our online trading or transaction processing systems may cause unanticipated system disruptions, slower response times, degradation in levels of customer service and impaired quality and speed of trade processing, any of which could have a material adverse effect on our business and operating results.

Our business and operations would suffer in the event of system failures.

Our success, in particular our ability to successfully facilitate bandwidth and derivative trades and provide high quality customer service, largely depends on the efficient and uninterrupted operation of our computer and communications hardware systems. Our systems and operations are vulnerable to damage or interruption from fire, flood, power loss, telecommunication failures, break-ins, earthquake and similar events. Despite the implementation of network security measures and redundancy, our servers are vulnerable to computer viruses, physical or electronic break-ins and similar disruptions, which could lead to interruptions, delays, loss of data or the inability to accept and fulfill customer orders.

If we do not respond effectively to technological change, our service could become obsolete and our business will suffer.

To remain competitive, we must continue to enhance and improve the responsiveness, functionality and features of the RateXchange Trading System and. The Internet and the online commerce industry are characterized by rapid technological change, changes in user and customer requirements and preferences, frequent new product and service introductions embodying new technologies and the emergence of new industry standards and practices that could render our existing systems and proprietary technology obsolete. Our success will depend, in part, on our ability to license leading technologies useful in our business, enhance our existing services, develop new services and technology that address the increasingly sophisticated and varied needs of our prospective customers, and respond to technological advances and emerging industry standards and practices on a cost-effective and timely basis.

The development of the RateXchange Trading System and other proprietary technology entails significant technical and business risks. There can be no assurance that we will successfully use new technologies effectively or adapt our systems and proprietary technology to user requirements or emerging industry standards. Our failure to adapt in a timely manner for technical, legal, financial or other reasons, to changing market conditions or customer requirements, could have a material adverse effect on our business and results of operations.

If we do not effectively manage growth, our ability to provide trading services will suffer.

To manage the expected growth of our operations and personnel, we will be required to improve existing, and implement new, transaction-processing, operational and financial systems, procedures and controls, and to expand, train and manage a growing employee base. Further, we will be required to maintain and expand our relationships with various hardware and software vendors, Internet and other online service providers and other third parties necessary to our business. If we are unable to manage growth effectively, we will be materially adversely affected.

We need to hire and retain qualified personnel to sustain our business.

We are currently managed by a small number of key management and operating personnel. We do not maintain "key man" insurance on any employee. Our future success depends, in part, on the continued service of our key executive, management and technical personnel, many of whom have recently been hired, and our ability to attract highly skilled employees. If any key officer or employee were unable or unwilling to continue in his or her present position, our business could be harmed. From time to time we have experienced, and we expect to continue to experience, difficulty in hiring and retaining highly skilled employees. If we are unable to retain our key employees or attract, assimilate or retain other highly qualified employees in the future, that may have a material adverse effect on our business and results of operations.

Our success is dependent on our ability to protect our intellectual property.

Our performance and ability to compete is dependent to a significant degree on our proprietary technology, including, but not limited to the design of the RateXchange Trading System. We regard our copyrighted material, software design, trade secrets and similar intellectual property as critical to our success, and we rely on trademark and copyright laws, trade secret protection and confidentiality and/or license agreements with our employees, customers, partners and others to protect our proprietary rights. We cannot assure you that we will be able to secure significant protection for any of our intellectual property. It is possible that our competitors or others will adopt product or service names similar to our marks, thereby inhibiting our ability to build brand identity and possibly leading to customer confusion.

We generally have entered into agreements containing confidentiality and non-disclosure provisions with our employees and consultants who have limited access to and distribution of our software, documentation and other proprietary information. We cannot assure you that the steps we take will prevent misappropriation of our technology or that agreements entered into for that purpose will be enforceable. Notwithstanding the precautions we have taken, it might be possible for a third party to copy or otherwise obtain and use our software independently. Policing unauthorized use of our technology is difficult, particularly because the global nature of the Internet makes it difficult to control the ultimate destination or security of software or other data transmitted. The laws of other countries may afford us little or no effective protection of our intellectual property.

Effective trademark, service mark, copyright and trade secret protection may not be available in every country where our services are made available online. In the future, we may also need to file lawsuits to enforce our intellectual property rights, protect our trade secrets and determine the validity and scope of the proprietary rights of others. Such litigation, whether successful or unsuccessful, could result in substantial costs and diversion of resources, which could have a material adverse effect on our business and operating results.

The volatility of our securities prices may increase.

The market price of our common stock has in the past been, and may in the future continue to be, volatile. A variety of events may cause the market price of our common stock to fluctuate significantly, including:

- Quarter to quarter variations in operating results;
- Adverse news announcements;
- The introduction of new products and services;
- Market conditions in the telecommunications industry in general, Internet-based services and commodity voice brokerage; and
- General market conditions.

In addition, the stock market in recent years has experienced significant price and volume fluctuations that have particularly affected the market prices of equity securities of many companies in our business and that often have been unrelated to the operating performance of such companies. These market fluctuations have adversely impacted the price of our common stock and may do so in the future.

Any exercise of outstanding options and warrants will dilute then-existing stockholders' percentage of ownership of our common stock.

We have a significant number of outstanding options and warrants. The exercise of all of the outstanding options and warrants would dilute the then-existing stockholders' percentage ownership of our common stock. Any sales resulting from the exercise of options and warrants in the public market could adversely affect prevailing market prices for our common stock. Moreover, our ability to obtain additional equity capital could be adversely affected since the holders of outstanding options and warrants may exercise their options and warrants at a time when we would also wish to enter the market to obtain capital on terms more favorable than those provided by the options. We lack control over the timing of any exercise or the number of shares issued or sold if exercises occur.

ITEM 3 QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Short Term Investments

Our exposure to market risks for changes in interest rates relate primarily to investments in debt securities issued by U.S. government agencies and corporate debt securities. We place our investments with high credit quality issuers and, by policy, limit the amount of the credit exposure to any one issuer.

Our general policy is to limit the risk of principal loss and ensure the safety of invested funds by limiting market and credit risk. All highly liquid investments with less than three months to maturity are considered to be cash equivalents. Investments with maturities between three and twelve months are considered to be short-term investments. Investments with maturities in excess of twelve months are considered to be long-term investments. We do not expect any material loss with respect to our short-term investment portfolio.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings.

Switch & Data Facilities Company v. RateXchange Corporation

In August of 2001 this action was dismissed following settlement of the claims. In exchange for a full release and the dismissal, the Company paid $250,000 in cash and issued 200,000 shares of restricted common stock to Switch & Data.

Martin v. RateXchange

On October 3, 2001, Gregory Martin and Patricia Whitney filed a lawsuit against RateXchange Corporation in the United States District Court for the Western District of Washington, C01-1565R alleging breach of contract. In 1998, Mr. Martin was the President and CEO of NetAmerica International Corporation (NAMI), a predecessor of RateXchange Corporation. In December of 1998 Mr. Martin was terminated from his employment with NAMI. The claims allege breach of agreements associated with Mr. Martin's employment. The complaint asks for damages of approximately $150,000.

Mr. Martin had filed suit previously in the Washington State court. That matter was dismissed following a settlement in May of 1999. Mr. Martin has now revived his claim against the Company.

The Company was recently served with the lawsuit and has not yet responded in court.

YellowBrix, Inc. v. RateXchange Corporation

On October 2, 2001, YellowBrix, Inc. filed a lawsuit against RateXchange Corporation in the Circuit Court for the City of Alexandria, Virginia alleging breach of contract. YellowBrix, Inc. provided news wire information to the Company in 2001. The complaint asks for damages of approximately $32,000. The Company was recently served with the lawsuit and has not yet responded in court.

RateXchange, Inc. v. PWREF/MCC-China Basin, LLC

In September of 2001, the RateXchange, Inc., one of the Company's Delaware subsidiaries, filed a lawsuit against PWREF/MCC-China Basin, LLC, its previous landlord, alleging constructive eviction and seeking declaratory relief. The allegations of the complaint arise from the lease for commercial space between the parties for the property located at 185 Berry Street, in San Francisco, California. PWREF/MCC-China Basin, LLC has recently responded to the complaint and filed a cross-complaint against RateXchange, Inc. The Company has reserved $132,000 to address this matter.

Based upon the facts known to the Company at this time and the applicable law, RateXchange does not expect the above cases to result in significant exposure to the Company and the Company has not set aside any additional reserves for the contingencies listed above.

Item 2. Changes in Securities and Use of Proceeds.

a) Not applicable.

b) Not applicable.

c) Not applicable

d) Not applicable.

Item 3. Exhibits and Reports on Form 8-K

Exhibits

4.1 Certificate of Designation of Series A Convertible Preferred Stock

Form 8-K

none

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized. Dated this 12th day of November, 2001.

RATEXCHANGE CORPORATION

By: /s/ D. Jonathan Merriman

D. Jonathan Merriman
Chairman and Chief Executive Officer