PERFORMANCE

Business review

Results overview

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS, EXCEPT PER SHARE AND PER ADS AMOUNTS)	2008 NZ$M	2007 NZ$M	2006 NZ$M	2005 NZ$M
Income statement data				
Operating revenues and other gains				
Local service	1,129	1,084	1,081	1,101
Calling	1,233	1,336	1,385	1,435
Interconnection	178	187	201	203
Mobile	833	895	869	835
Data	638	561	602	602
Broadband and internet	547	485	448	376
IT services	439	380	346	308
Other operating revenues	669	634	563	550
Other gains	7	20	60	154
Total operating revenues and other gains	**5,673**	**5,582**	**5,555**	**5,564**
Operating expenses				
Labour	886	773	760	705
Intercarrier costs	1,243	1,220	1,199	1,185
Other operating expenses	1,653	1,603	1,497	1,417
Impairment	-	-	1,301	24
Other expenses	-	52	34	35
Depreciation and amortisation	761	652	699	692
Total operating expenses	**4,543**	**4,300**	**5,490**	**4,058**
Net earnings/(loss) from continuing operations	713	844	(540)	874
Net earnings from discontinued operations[1]	-	2,183	109	96
Net earnings/(loss) attributable to shareholders	710	3,024	(435)	967
Earnings/(loss) per share/ADS from continuing operations[2]				
Basic per share	0.38	0.42	(0.28)	0.45
Diluted per share	0.38	0.42	(0.28)	0.44
Basic per ADS	1.90	3.39	(2.20)	3.59
Diluted per ADS	1.90	3.36	(2.20)	3.54
Earnings/(loss) per share/ADS from discontinued operations[2]				
Basic per share	-	1.10	0.06	0.05
Diluted per share	-	1.08	0.06	0.05
Basic per ADS	-	8.78	0.44	0.39
Diluted per ADS	-	8.64	0.44	0.39
Net earnings/(loss) per share/ADS[2]				
Basic per share	0.38	1.52	(0.22)	0.50
Diluted per share	0.38	1.50	(0.22)	0.49
Basic per ADS	1.90	12.16	(1.78)	3.97
Diluted per ADS	1.90	11.96	(1.78)	3.91
Balance Sheet Data				
Property, plant and equipment	3,984	3,681	3,301	3,602
Total assets	7,405	8,276	6,203	7,504
Debt due within one year	958	488	955	863
Long-term debt	1,830	2,404	2,543	2,973
Total liabilities	4,669	4,672	5,141	5,033
Total equity	2,736	3,604	1,062	2,471
Contributed capital	1,297	2,270	2,011	1,991
Weighted average number of ordinary shares outstanding				
Basic (in millions)	1,871	1,990	1,960	1,948
Diluted (in millions)	1,873	2,026	1,960	2,027

1 Earnings from discontinued operations consist of the net earnings of Yellow Pages Group after taxation and includes the profit on disposal of NZ$2,084 million in 2007.

2 Per share amounts have been calculated as earnings/(loss) divided by the weighted average number of shares outstanding during the periods indicated. Per ADS amounts have been calculated based on a ratio of five shares per ADS for 2008 and eight shares per ADS for prior years. See the discussion on liquidity and capital resources for an explanation of the change in the ratio of ADS during 2008. Accordingly, per ADS information for 2008 is not comparable to per ADS information for the prior years due to the change in ADS ratio. Diluted earnings per share and per ADS amounts reflect the dilutive effects of options and capital securities.

3 Telecom's financial results are prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board. 2005 was Telecom's first year of reporting under IFRS therefore the summary financial information above excludes 2004.

Group result

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Operating revenues and other gains	5,673	5,582	5,555	1.6	0.5
Labour	(886)	(773)	(760)	14.6	1.7
Intercarrier costs	(1,243)	(1,220)	(1,199)	1.9	1.8
Other operating expenses	(1,653)	(1,603)	(1,497)	3.1	7.1
Impairment	-	-	(1,301)	-	(100.0)
Other expenses	-	(52)	(34)	(100.0)	52.9
Depreciation	(574)	(500)	(536)	14.8	(6.7)
Amortisation	(187)	(152)	(163)	23.0	(6.7)
Total operating expenses	(4,543)	(4,300)	(5,490)	5.7	(21.7)
Finance income	119	59	28	101.7	110.7
Finance expense	(271)	(289)	(282)	(6.2)	2.5
Share of associates' losses	(3)	(3)	-	-	NM[1]
Net earnings/(loss) before income tax	**975**	**1,049**	**(189)**	(7.1)	NM[1]
Income tax expense	(262)	(205)	(351)	27.8	(41.6)
Net earnings/(loss) from continuing operations	**713**	**844**	**(540)**	(15.5)	NM[1]
Net earnings from discontinued operations	-	2,183	109	NM[1]	NM[1]
Net earnings/(loss) for the year	**713**	**3,027**	**(431)**	(76.4)	NM[1]
Net earnings/(loss) attributable to shareholders	710	3,024	(435)	(76.5)	NM[1]
Minority interests in earnings of subsidiaries	3	3	4	-	(25.0)
Net earnings/(loss) for the year	**713**	**3,027**	**(431)**	(76.4)	NM[1]

1 Not meaningful

Executive summary

In 2008 Telecom's retail market share and profit margin declined in New Zealand with fixed line losses accelerating and mobile revenues declining. There has been significant growth in broadband penetration and ICT services in the New Zealand market. These trends in the New Zealand market are not unique, they have happened all around the world, and emphasise the need for Telecom to transform its business. Telecom's Australian business has made progress in the integration of AAPT and PowerTel, which is largely complete. However, as expected, the benefits of the integration were offset by integration costs in the first year and these benefits have not resulted in a significant improvement in the segment result of the Australian business that was a loss for 2008.

In 2008 operating revenues and other gains increased by NZ$91 million (1.6%) compared to 2007. Operating revenue increased in the areas of local service, data, broadband and internet, IT services and other operating revenue. However, these increases were partially offset by decreases in calling, interconnection, mobile and other gains. Local service revenue increased by NZ$45 million primarily due to 2008 being the first full year of PowerTel revenues following the acquisition of PowerTel by Telecom in May 2007 but this effect was partially offset by the decline in local service revenue for the New Zealand operations due to a decline in customers. Broadband and internet revenue increased by NZ$62 million (12.8%) when compared to 2007 as a result of continued connection growth. Total broadband connections at 30 June 2008 were 759,000 for New Zealand (30 June 2007: 605,000) and 157,000 for Australia (30 June 2007: 174,000). IT services revenue increased by NZ$59 million (15.5%) principally due to the growth in IT services arising from market share gains with major customers. Offsetting these growth areas, increased competitive pressure in New Zealand led to a decline in calling revenues of NZ$103 million (7.7%) compounded by decreased calls to mobile networks in the Australian market. Mobile revenue decreased by NZ$62 million (6.9%) due to the impact of lower pricing, reduced calling volumes and a decline in handset revenue.

Operating expenses increased in 2008 by NZ$243 million (5.7%) from 2007. Labour costs increased by NZ$113 million (14.6%) as a result of increased personnel costs in both New Zealand and Australia due to increased staffing needs to deliver on the IT services contracts won by Gen-i, the effect of a full year of PowerTel's costs, focus on the transformation programmes, and implementing operational separation requirements across all separated divisions in New Zealand, compounded by salary pressure incurred in tight labour markets. Depreciation and amortisation expense increased in 2008 by NZ$109 million (16.7%) from 2007 as a result of the full year effect of PowerTel in the group's results, the increase in capital expenditure on telecommunications hardware and software in previous periods and accelerated depreciation in certain asset categories. Finance income was NZ$60 million higher than 2007 due to the investment of the proceeds from the sale of Yellow Pages Group. Tax expense was higher in 2008 than 2007 due to the tax credits that were recognised in 2007.

In 2007 operating revenues and other gains increased by NZ$27 million (0.5%) from 2006. There was growth in mobile revenue

as a result of growth in the customer base and penetration of mobile data services, continued growth in broadband and internet revenue, reflecting increased broadband penetration and strong growth in IT services revenue. Other operating revenue also increased, principally driven by growth in resale revenue in Australian Operations. Growth across these revenue categories was partly offset by lower calling, data and interconnection revenues.

Excluding impairment, operating expenses increased in 2007 from 2006 largely as a result of growth in sales costs associated with the growth in IT services and the broadband customer base in New Zealand. The impairment in 2006 related to the write-down of Telecom's Australian operations. Depreciation and amortisation expense declined in 2007 compared to 2006 as a result of the write-down of Australian operations' tangible assets in 2006. Net interest expense decreased in 2007 compared to 2006 due to the receipt of the proceeds from the sale of Yellow Pages Group, while tax expense was significantly impacted by the recognition of deferred tax benefits resulting from the previous write-down of Australian operations. Excluding the credit for the deferred tax benefit on the write-down, the effective tax rate for 2007 was 29.1%. This was slightly lower than the New Zealand corporate tax rate of 33% partly due to a non-assessable gain on the sale of Telecom Samoa Cellular Limited.

Principal factors impacting Telecom's results and key trends

Increased regulation

As described in the Regulation section of this annual report, Telecom has been subject to increasing regulation in recent years and operates in a regulatory environment where the regulator sets determinations on the pricing of regulated services, such as UCLL and UBA. The introduction of these new regulated services is likely to have the effect of accelerating the rate of broadband penetration, yet may result in further downward pressure on wholesale and retail broadband prices due to increased competition. More importantly, UCLL and UBA pose threats to Telecom's retail fixed line access relationship with customers and could accelerate the rate of decline in traditional access and calling services as Telecom loses the fixed line access relationship with the customer when a competitor supplies UCLL or UBA directly. Telecom Wholesale's revenues should continue to increase given the growth expected in the broadband market but any downwards pressure on the regulated prices would result in a reduction of revenue and increase retail competition for Telecom.

Transformation programmes

Telecom has committed to transform its business in response to increased regulation and its declining profit margins.

During the year Telecom separated its retail, wholesale and network business units (as detailed in the 'Regulation' section of this annual report). This has led to increased operating expenses to implement these changes and has also consumed a substantial amount of management time and effort. Telecom expects that operational separation will continue to drive additional costs, both operating and capital, into the business. Telecom incurred incremental operating costs of NZ$24 million during 2008 and capital expenditure of NZ$29 million. It has become increasingly difficult to distinguish between incremental costs specifically driven by operational separation as it becomes part of business as usual. It is therefore unlikely that these costs can be reported separately in future periods.

Concurrent with the organisational transformation, Telecom has embarked on three major capital transformation programmes, as detailed in 'Strategy', to deploy fibre, build a new mobile network and complete the next generation network. These programmes have increased, and will continue to increase, consumption of labour resources and capital expenditure in the short term, however, in the long term should lead to a more efficient operating model with new revenue streams and lower network costs as Telecom is able to retire legacy systems and implement a lower cost IP platform.
For 2009, Telecom currently expects that capital expenditure will be up to NZ$1,100 million as Telecom delivers on its transformation strategies. This is principally due to the expected expenditure on the WCDMA network, the fibre rollout and spending on next generation Telecom capability.

Declining profit margins

Telecom's net earnings in New Zealand have declined due to a fall in traditional revenues partially offset by an increase in lower margin IT services revenues. Traditional revenues have declined due to increased competition and technological changes requiring new investments and product substitution. IT services revenues, whilst a key growth area for Telecom in New Zealand and Australia, have lower margins (and lower capital expenditure requirements) than traditional revenue streams. In addition, securing new customers has led to a significant increase in operating expenditures in both labour and operating expenses due to the staffing and direct costs required to service these contracts.

Telecom has also continued to increase its penetration in the New Zealand broadband market. This has been achieved through competitive pricing and customer inducements, such as free modems, that have upfront costs associated with each customer acquisition. Once the rate of penetration in the broadband market slows, these upfront costs should decline.

Australian operations

Telecom purchased PowerTel in May 2007, hence Telecom's segmental results for Australia are not comparable for 2008 and 2007. PowerTel has invested heavily in the development of an extensive telecommunications network, which has seen it emerge predominantly as a wholesale provider. AAPT's recent investment in an IT platform to enable the provision of an improved customer experience, the Hyperbaric project, has focused on the service layer in order to position it in the SME and mass-market segments. Accordingly, Telecom believes that the operations of the two entities are complementary and significant integration benefits are anticipated from combining the two entities. The integration of AAPT and PowerTel is

largely complete, and there is now an ongoing focus on selling profitable on-net data and internet services.

These benefits should offset the trends Telecom has experienced in Australia over the three-year period where retail prices have continued to decline across most product categories. Within its Australian operations, Telecom has a very small share of the overall telecommunications market and margins remain under significant pressure, which have contributed to the Australian operations segment result being a loss. Competition from larger competitors has restricted Telecom's ability to acquire new customers, particularly in the corporate and large business sector, and has also put significant downwards pressure on prices.

Decline in mobile revenues

The New Zealand mobile market has undergone significant expansion over the last three years. Telecom's New Zealand mobile customer base has risen from 1,601,000 customers at 30 June 2005 to 2,176,000 customers at 30 June 2008, but saturation in the New Zealand market and a decision to cease selling standalone mobile packages in the Australian market have led to a decline in handset sales and a decline in traditional mobile voice revenues.

Telstra's decision to close its CDMA network in Australia in April 2008 had a negative impact on Telecom's roaming proposition as its New Zealand mobile customers could not roam on their CDMA phones in Australia. As an interim solution Telecom introduced WorldMode phones that have the ability to roam on both CDMA and GSM networks and a long-term solution will be the rollout of a WCDMA network. These trends have led to a decline in mobile revenue in 2008 and a significant increase in capital expenditure to launch a new mobile network. The new WCDMA network should enable higher average revenue per user as it supports enhanced commercial and consumer services, including high quality music, video and entertainment offerings, as well as allowing Telecom to capture a share of mobile outbound and inbound roaming revenue.

In December 2007 Vodafone and NZ Communications announced they had signed a deal to provide NZ Communications with national roaming services, indicating that a third mobile entrant in the New Zealand market is likely. A new mobile entrant would place further downward pressure on any future growth in mobile revenues and mobile profit margins.

Increase in wholesale revenues

Telecom's wholesale revenues have benefited from the increased competition in the New Zealand market. An increase in wholesale activity leads to a decline in Telecom's retail calling, broadband and data revenues as customers will have their calling, broadband and data services supplied by competitors.

Southern Cross dividends

Telecom received NZ$89 million of dividends from Southern Cross in 2008. These dividends are made as a result of Southern Cross selling capacity in its cable, and future dividends are contingent upon future sales. Southern Cross is currently the largest supplier in the market for capacity between Australasia and the US. New entrants to that market are expected in 2009 and 2010 that would reduce Southern Cross' share of the market. In addition, the emergence of multi-cable competition is already driving capacity prices down. Southern Cross has responded to this competition and has recently doubled its capacity, funding the upgrade out of its cash flow. This upgrade should allow Southern Cross to compete with the new cables and ongoing dividends are expected, with the current estimate being NZ$40 to NZ$60 million for 2009.

Depreciation and amortisation

Depreciation and amortisation represents a significant component of Telecom's operating expenses, given the major investment in capital equipment required to support its operations.

The level of capital expenditure impacts on depreciation and amortisation expense. Annual capital expenditure is currently in excess of the annual depreciation and amortisation and this is expected to be the case again in the 2009 financial year. This will ultimately flow through to higher depreciation and amortisation charges in future periods.

Other than capital expenditure, depreciation has been impacted by the acquisition of PowerTel in May 2007, where the amount of Australian depreciation increased in 2008 by NZ$52 million, while the significant impairment recognised in respect of Australian operations in 2006 reduced the Australian depreciation charge in 2007.

Disposal of Yellow Pages Group

In April 2007, Telecom completed a competitive sales process that resulted in the sale of Yellow Pages Group for NZ$2,161 million (see note 36 to the financial statements for more detail). In accordance with NZ IFRS, the operating results of Yellow Pages Group and the net gain on sale is presented in Telecom's financial statements as results from discontinued operations. NZ$1,113 million of the NZ$2,161 million that Telecom received from the sale was returned to shareholders in October 2007 as part of a capital return by way of a court-approved pro-rata share cancellation.

Outlook

Telecom has indicated that management does not foresee a return to earnings before interest, taxation, depreciation and amortisation expenses (EBITDA) growth until 2011, when Telecom expects to see the benefits of its strategy and transformation programmes coming to fruition. Telecom expects EBITDA to decline by 4% to 6% in 2009 and continue to decline until 2011.

Telecom expects that capital expenditure will reach a peak in 2009 of up to NZ$1,100 million as Telecom delivers on its transformation strategies. This is based on Telecom's current technology plans and, as noted in Group Risk Factors, could potentially increase depending on which WCDMA solution is chosen.

In the short term Telecom currently expects the following outcomes for the year ending 30 June 2009:

- Group EBITDA to decline by 4% to 6%
- EBITDA from AAPT of A$70 million to A$90 million

- Dividends from Southern Cross of between NZ$40 million to NZ$60 million
- Group depreciation and amortisation of NZ$870 million to NZ$920 million
- Group capital expenditure up to NZ$1,100 million
- Group consolidated net earnings after tax of NZ$500 million to NZ$540 million.

It is important to understand that this outlook is based on a number of assumptions, including, without limitation Telecom's ability to successfully transform its business, including its ability to implement its NGT business model and NGN, and its ability to reduce costs.

In addition, this outlook is based on the current regulatory environment and market and competitive conditions, which are expected to change over time. Accordingly, this outlook is subject to material change. Telecom's ability to achieve the outlook in this section and the annual report is subject to significant risks. See 'Group Risk Factors' for a description of the key risks and the 'Forward-looking Statements' section.

Earnings before interest, taxation, depreciation and amortisation (EBITDA)

Telecom uses EBITDA, a non-GAAP measure, when discussing group results and in giving future performance guidance. Management believes that this measure provides useful information as it is used internally to evaluate performance of business units, to analyse trends in cash-based expenses, to establish operational goals and allocate resources. Telecom calculates EBITDA by adding back depreciation, amortisation, finance expense, share of associates' losses and taxation expense to net earnings/(loss) from continuing operations less finance income.

EBITDA is a non-GAAP financial measure and is not prepared in accordance with IFRS. It is not uniformly defined or utilised by all companies in the telecommunications industry. Accordingly, this measure may not be comparable with similarly titled measures used by other companies. Non-GAAP financial measures should not be viewed in isolation, nor considered as a substitute for measures reported in accordance with IFRS.

The calculation of Telecom's EBITDA and its reconciliation to the IFRS measure of net earnings/(loss) from continuing operations is shown below.

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/2007 % CHANGE	2007/2006 % CHANGE
Net earnings/(loss) from continuing operations	713	844	(540)	(15.5)	NM[1]
Add back: depreciation	574	500	536	14.8	(6.7)
Add back: amortisation	187	152	163	23.0	(6.7)
Less: finance income	(119)	(59)	(28)	101.7	110.7
Add back: finance expense	271	289	282	(6.2)	2.5
Add back: share of associates' losses	3	3	-	-	NM[1]
Add back: taxation expense	262	205	351	27.8	(41.6)
EBITDA	1,891	1,934	764	(2.2)	153.1

1 Not meaningful

Operating results

Revenue

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Local service	1,129	1,084	1,081	4.2	0.3
Calling	1,233	1,336	1,385	(7.7)	(3.5)
Interconnection	178	187	201	(4.8)	(7.0)
Mobile	833	895	869	(6.9)	3.0
Data	638	561	602	13.7	(6.8)
Broadband and internet	547	485	448	12.8	8.3
IT services	439	380	346	15.5	9.8
Other operating revenues	669	634	563	5.5	12.6
Other gains	7	20	60	(65.0)	(66.7)
Operating revenues and other gains	**5,673**	**5,582**	**5,555**	1.6	0.5

Local service

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Business and residential access	958	925	914	3.6	1.2
Local calls	87	85	93	2.4	(8.6)
Smartphone, messaging and call track	84	74	74	13.5	-
Total local service revenues	**1,129**	**1,084**	**1,081**	4.2	0.3

Local service revenues primarily consist of business and residential access revenue. In 2008 revenue increased by NZ$45 million (4.2%) from 2007 due to the inclusion of PowerTel revenues for the full year following the acquisition of PowerTel in May 2007, offset by a decline of NZ$16 million in New Zealand local services revenues due to lower local calls, migration of dial-up internet to broadband, use of VoIP products and substitution to mobile. The number of total access lines has continued to decline due to mobile substitution and slowing housing growth.

Local service revenues were stable in 2007 compared to 2006 as the increase in access revenues, from an increase in line rental charge in March 2006, was offset by a decrease in local call revenues. The decline in local call revenues was due largely to businesses migrating from dial-up internet access to broadband and declining call volumes as a result of competitive pressure.

Calling

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
National	753	816	897	(7.7)	(9.0)
International	432	472	442	(8.5)	6.8
Other	48	48	46	-	4.3
Total calling revenue	**1,233**	**1,336**	**1,385**	(7.7)	(3.5)

Calling revenue includes gross transit revenue that fluctuates with the associated transit costs. Excluding transit revenues, calling revenue declined NZ$90 million (8.1%) in 2008 and NZ$94 million (7.4%) in 2007.

National calling revenue (including national calls, calls to mobile networks and national 0800) decreased by NZ$144 million across the three-year period to 30 June 2008 due to the migration of residential customers to wholesale competitors and lower average prices due to retail customer adoption of subscription-based calling plans offered by Telecom. These factors led to the decline in 2008 of national revenues to NZ$753 million from NZ$816 million in 2007.

In 2007 revenue from national calling decreased by NZ$81 million when compared to 2006 with volumes 13% lower largely due to fixed-to-mobile substitution, with a related increase in volume in mobile calls and calls to mobile networks. Revenue from calls to mobile networks fell as average prices decreased, partly offset by an increase in call minutes.

International calling revenue for New Zealand comprises outward calling revenue, where New Zealand customers make calls from fixed networks originating in New Zealand and terminating overseas; inwards calling revenue, where calls originated by overseas carriers terminate on Telecom's fixed or mobile networks or calls terminating on other companies' networks; and transit calling revenue, where Telecom acts as an intermediary carrier of international calls.

In 2008 international calling revenue decreased by NZ$40 million (8.5%) from 2007 due to declining outward calling revenue and transit revenue. International outward calling revenues declined in 2008 due to product substitution and price competition. The amount of international transit revenues earned depends on the prevailing foreign exchange rates (principally the US dollar) as well as destination blend. International transit revenues decreased in 2008 compared to 2007. This has largely been mirrored by the movement in the related intercarrier costs, which decreased by NZ$14 million. The net margin from international transits was unchanged at NZ$38 million for both 2008 and 2007.

In 2007 international calling revenue increased by NZ$30 million compared to 2006 due to an increase in international transit revenues as a result of increased volumes, offset by a decrease in outwards calling revenue due to declining average prices.

Interconnection

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
PSTN interconnection	105	109	109	(3.7)	-
Mobile interconnection	73	78	92	(6.4)	(15.2)
Total interconnection revenue	**178**	**187**	**201**	(4.8)	(7.0)

Interconnection revenue declined by NZ$9 million (4.8%) in 2008 due to a decrease in PSTN interconnections and a decrease in mobile interconnect revenue, which was a result of a decrease in termination rates with a corresponding decrease in intercarrier costs.

Interconnection revenue decreased in 2007 principally due to a reduction in revenue billed to interconnection carriers, with a corresponding decrease in intercarrier costs due to a decrease in termination rates.

Mobile

Mobile revenues YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Voice	543	589	610	(7.8)	(3.4)
Data	233	224	174	4.0	28.7
Other	57	82	85	(30.5)	(3.5)
Total mobile revenue	**833**	**895**	**869**	**(6.9)**	**3.0**

Mobile connections AS AT 30 JUNE	2008 000's	2007 000's	2006 000's	2008/07 % CHANGE	2007/06 % CHANGE
New Zealand	2,176	1,977	1,703	10.1	16.1
Australia	85	150	162	(43.3)	(7.4)

2008 mobile revenue was NZ$833 million representing a decrease of NZ$62 million (6.9%) from 2007 due to a decline in handset revenue, reduced calling volumes and the impact of new pricing offers. Voice revenue decreased by NZ$46 million (7.8%) as a result of the impact of new pricing offers despite growth in total connections. Mobile data revenue increased by NZ$9 million (4.0%) as a result of increased volumes, primarily in wireless broadband. Other mobile revenues decreased by NZ$25 million (30.5%) due to a decline in the number of handsets sold due to competitive pressure.

Mobile revenue excludes any revenue from terminating calls and text messaging from competitors' networks, which is included in interconnection revenue.

The mobile market is extremely competitive but Telecom has seen the number of mobile customers increase over 2008; however there is a continued trend of falling demand for voice services but an increasing demand for data services. Telecom's New Zealand mobile connections grew by 199,000 in 2008 (30 June 2007: 274,000) to reach 2,176,000 at 30 June 2008. Of the 30 June 2008 total connections, 39% were post-paid connections, and 61% were prepaid (30 June 2007: 41% post-paid, 59% prepaid).

Future mobile data revenue growth is expected to be driven by growth in applications and content. As an integrated operator, Telecom is focused on the convergence of fixed and mobile services, which is seen as a potential growth area. The mobile market is also the subject of growing regulation; one result of that may well be an increase in wholesale mobile virtual network operator (MVNO) models.

Mobile revenues were up 3% in 2007 compared to 2006 to NZ$895 million led by an increase of NZ$50 million in mobile data revenues driven by volume increases as described above. While the overall number of mobile connections grew by 274,000 to nearly 2 million in New Zealand, mobile voice revenues fell by 3.4% to NZ$589 million as a result of lower average prices per call and a decline in the number of mobile connections in Australia. Other mobile revenue remained relatively stable.

Average Revenue Per User (ARPU)
Telecom uses ARPU within its New Zealand operations to measure the average monthly service revenue on a per-customer basis. Management believes that this measure provides useful information about the usage of Telecom's products and the company's ability to attract and retain high value customers. Telecom calculates ARPU as mobile voice and data revenue for the year divided by the average number of customers for the year. This is then divided by 12 to express the result as a monthly figure. The revenues that Telecom uses in calculating ARPU exclude revenues from handset and accessory sales, as these are not ongoing customer revenue streams, and paging revenue, inwards roaming and other miscellaneous mobile revenues, as these are not generated by Telecom's mobile customers. As calculated by Telecom, ARPU also excludes any revenue from terminating fixed to mobile calls (which is included in interconnection revenue).

ARPU is a non-GAAP financial measure and is not prepared in accordance with IFRS. It is not uniformly defined or utilised by all companies in the telecommunications industry. Accordingly,

this measure may not be comparable with similarly titled measures used by other companies. Non-GAAP financial measures should not be viewed in isolation or considered as a substitute for measures reported in accordance with IFRS.

The calculation of Telecom's mobile ARPU and its reconciliation to the IFRS measure of mobile revenue is shown below.

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Total mobile revenue (NZ$m)	833	895	869	(6.9)	3.0
Less handset sales and non-customer revenues (NZ$m)	(57)	(82)	(85)	(30.5)	(3.5)
Less Australian mobile voice and data revenue (NZ$m)	(55)	(73)	(87)	(24.7)	(16.1)
New Zealand mobile voice and data revenue (NZ$m)	721	740	697	(2.6)	6.2
Average customers in New Zealand (000's)	2,077	1,845	1,723	12.6	7.1
ARPU (NZ$ per month)	**28.93**	**33.42**	**33.71**	(13.4)	(0.9)

ARPU decreased by 13.4% in 2008 compared to 2007 primarily due to the impact of competition on pricing and the dilutive impact of the integrated call plan offering without access fees. Telecom has lowered pricing on postpaid plans in response to competition in the New Zealand market to attract and retain customers. Voice revenues were lower due to lower roaming revenues in Australia following the closure of the Telstra CDMA network in Australia in April 2008, and discounted pricing offers on global roaming. Prepaid plans have also been subject to lower pricing due to competition, and Telecom increased the monthly text cap on certain prepaid plans, which resulted in lower data revenues.

ARPU was stable in 2007 compared to 2006 due to a combination of increased data revenues and the removal of inactive connections from the TDMA customer base in 2006. The TDMA network was closed on 31 March 2007. All mobile customers are now on the CDMA network.

Data

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Managed IP data services	233	215	293	8.4	(26.6)
Traditional data services	405	346	309	17.1	12.0
Total data revenues	**638**	**561**	**602**	13.7	(6.8)

Data revenues arise from meeting customers' non-voice communications needs. There has been a shift away from traditional dedicated circuit, leased line data products towards IP-based data products given the increased flexibility and cost-efficiency that these products offer.

In 2008, data revenues increased due to the inclusion of PowerTel revenues for the full year. Outside of the PowerTel related increase, data revenues remained broadly stable, due to a decrease in traditional data services, offset by increased managed IP data services. In 2007 data revenues declined principally due to the effect of regulatory pricing in New Zealand and the loss of key corporate customers in Australia, compounded by price erosion on the negotiation of new contracts.

Broadband and internet

Broadband and internet revenue YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Broadband revenue	499	415	360	20.2	15.3
Internet revenue	36	51	70	(29.4)	(27.1)
Other	12	19	18	(36.8)	5.6
Total broadband and internet revenue	**547**	**485**	**448**	12.8	8.3

Broadband connections AS AT 30 JUNE	2008 000S	2007 000S	2006 000S	2008/07 % CHANGE	2007/06 % CHANGE
New Zealand	759	605	435	25.5	39.1
Australia	157	174	102	(9.8)	70.6

Active dial-up internet connections AS AT 30 JUNE	2008 000S	2007 000S	2006 000S	2008/07 % CHANGE	2007/06 % CHANGE
New Zealand	163	238	310	(31.5)	(23.2)
Australia	41	63	90	(34.9)	(30.0)

Broadband services in New Zealand continue to grow. Broadband connections at 30 June 2008 were 759,000 for New Zealand (30 June 2007: 605,000) and 157,000 for Australia (30 June 2007: 174,000). The 2008 revenue from broadband was NZ$499 million, reflecting an increase of 20.2% over 2007. Revenue from broadband has not grown to the same extent as the overall broadband customer base, largely because of downward price pressures, particularly in the business sector.

Internet revenue decreased due to the continued migration of customers from dial-up internet to broadband.

In 2007 broadband and internet revenue increased by NZ$37 million (8.3%) from 2006. While consumer broadband revenue grew, it was offset by a decline in business broadband revenue, driven by the realignment of prices for business customers in New Zealand to align them with consumer prices.

IT services

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
IT services	439	380	346	15.5	9.8
Total IT services revenue	**439**	**380**	**346**	15.5	9.8

IT services revenue includes provision of network-based application services, management of customers' information, communication and technology services and integration of these services.

IT services revenue increased by NZ$59 million (15.5%) to NZ$439 million in 2008 when compared to 2007, principally due to the growth in IT solutions revenue, procurement and network-delivered services as a result of strong growth in sales across a broad range of enterprise and corporate customers.

IT services revenue increased by NZ$34 million (9.8%) in 2007 due to similar organic growth.

Other operating revenue

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Resale	360	399	363	(9.8)	9.9
Dividends	89	19	-	NM[1]	NM[1]
Equipment sales	45	52	55	(13.5)	(5.5)
Other revenue	175	164	145	6.7	13.1
Total other operating revenue	**669**	**634**	**563**	5.5	12.6

1 Not meaningful

In 2008 resale revenue, derived in Australia, decreased by NZ$39 million (9.8%) when compared to 2007 as a result of a decline in customer numbers, partially offset by growth in wholesale resale revenue. Dividends increased in 2008 from 2007 due to dividends from Telecom's investment in Southern Cross.

In 2007 resale revenue increased by 9.9% compared to 2007 due to strong growth in revenue from business customers, coming primarily from wholesale operations, offset by decreases as a result of price reductions and price capping to retain market share in a very competitive market. Dividends received were also from Southern Cross.

Other gains

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Sale of mobile customer base in Australia	7			NM[1]	-
Sale of Telecom Samoa Celluar	-	20	-	(100.0)	NM[1]
Acquisition of Southern Cross Cables	-	-	60	-	(100.0)
Total other gains	**7**	**20**	**60**	(65.0)	(66.7)

1 Not meaningful

In July 2007 AAPT recorded a NZ$7 million gain from the sale of the standalone mobile customer base in Australia.

The gain recognised in 2007 of NZ$20 million relates to the gain arising on the disposal of Telecom Samoa Cellular Limited. The other gain in 2006 represents a gain of NZ$60 million pertaining to the acquisition of Southern Cross Cables (NZ) Limited whose sole asset at the time of acquisition was a tax operating loss carryforward. The value of this tax loss carryforward was NZ$70 million and Telecom's acquisition cost was NZ$10 million. The value in excess of Telecom's acquisition cost has been reflected as a gain.

Expenses

Labour

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
New Zealand	626	545	539	14.9	1.1
Australia	247	216	209	14.4	3.3
Other	13	12	12	8.3	-
Total labour expense	**886**	**773**	**760**	14.6	1.7

Labour expense increased by NZ$113 million (14.6%) in 2008. Personnel numbers increased in 2008. The increase in labour costs is a reflection of the increase in personnel supporting IT services, staffing of the transformation programmes, building up the wholesale business, implementing operational separation requirements and salary pressure incurred in a tight labour market. In Australia the increase reflects the inclusion of PowerTel for a full year following its acquisition in May 2007, as well as growth in the Gen-i head count. These increases were partly offset by outsourcing of call centres and synergies realised as a result of the AAPT/PowerTel merger.

In 2007 labour expense increased by NZ$13 million (1.7%) as personnel increased when compared to 2006. This increase in people reflected a move to build capability to support the IT programme and increased resources to support strategic initiatives. This increase was partially offset by the impact of an organisational change programme initiated in 2006.

Intercarrier costs

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
New Zealand	457	491	500	(6.9)	(1.8)
Australia	786	729	699	7.8	4.3
Total intercarrier costs	**1,243**	**1,220**	**1,199**	1.9	1.8

Intercarrier costs increased by NZ$23 million (1.9%) in 2008 when compared to 2007 due to the full year effect of PowerTel increasing the Australian costs, offset by a decline in costs in New Zealand consistent with the decline in New Zealand intercarrier revenues, as well as the translation effect from the strength of the NZ dollar on US dollar denominated intercarrier costs.

In 2007 the decrease in New Zealand intercarrier costs was due to lower mobile interconnections due to a reduction in revenue billed to interconnection carriers offset by an increase in international intercarrier costs, primarily due to growth in international transit volumes.

Telecom and Vodafone undertook in 2007 to reduce mobile termination rates over a five-year period and so it is likely that the cost to Telecom of interconnecting with other mobile operators will fall over this period (as will revenue for calls to mobile networks and mobile interconnection revenue).

Other operating expenses

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Direct costs	352	326	279	8.0	16.8
Mobile acquisitions, upgrades and dealer commissions	280	312	317	(10.3)	(1.6)
Procurement and IT services	264	222	180	18.9	23.3
Broadband and internet	67	80	73	(16.3)	9.6
Computer costs	197	194	162	1.5	19.8
Advertising, promotions and communications	90	129	143	(30.2)	(9.8)
Accommodation	127	111	105	14.4	5.7
Outsourcing	52	26	23	100.0	13.0
Travel	18	15	14	20.0	7.1
Provision for doubtful debts	29	33	34	(12.1)	(2.9)
Other	177	155	167	14.2	(7.2)
Total other operating expenses	**1,653**	**1,603**	**1,497**	3.1	7.1

In 2008 other operating expenses increased principally due to an increase in procurement and IT services costs and direct costs, offset by a decline in the cost of mobile acquisitions, upgrades and dealer commissions. Procurement and IT services costs increased by NZ$42 million due to the direct costs of fulfilling IT services contracts, revenue from which increased by NZ$59 million. Mobile acquisition, upgrades and dealer commissions declined due to a decrease in connection volumes. Accommodation increased due to the inclusion of the costs of PowerTel properties for 2008. Outsourcing costs increased due to the outsourcing of call centres in Australia.

In 2007 other operating expenses increased by NZ$106 million when compared to 2006. Direct costs increased largely due to increased provisioning costs associated with higher broadband connections as gross connections increased year-on-year and the cost of driving improvements in restoration performance. Mobile acquisitions, upgrades and dealer commissions increased due to increased connections volumes. IT services sales cost growth reflects growth in IT services revenue and a change in the sales mix towards products and services, with a larger proportion of sales costs rather than labour costs.

Impairment

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Impairment of Australian operations	-	-	1,301	-	(100.0)
Total impairment expense	**-**	**-**	**1,301**	-	(100.0)

Impairment charges totalling NZ$1,301 million were recognised in 2006 in respect of Telecom's Australian operations following a decline in value that was a consequence of a number of negative trends that adversely affected the short and long-term earnings outlook for Australian operations.

Other expenses

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Restructuring costs	-	36	-	(100.0)	NM[1]
Provision for billing issues	-	16	-	(100.0)	NM[1]
Intercarrier and regulatory costs	-	-	22	-	(100.0)
Provision for contractual settlements	-	-	12	-	(100.0)
Total other expenses	**-**	**52**	**34**	(100.0)	52.9

1 Not meaningful

In 2007 restructuring costs of NZ$36 million were recognised resulting from restructuring activities undertaken or announced in 2007, including a companywide organisational redesign programme, the costs of rationalising Australian call centre operations and the integration of PowerTel. A provision of NZ$16 million was recognised for the cost of rectifying several billing application configuration issues primarily relating to prior periods. The provision covers the cost of investigating and resolving these issues.

In 2006 expenses were recognised of NZ$22 million in relation to intercarrier and regulatory matters and NZ$12 million for the liability that resulted from unsuccessful outcomes relating to historic issues under the Fair Trading Act and the cost of terminating an agreement with Hutchison Whampoa.

Depreciation and amortisation

Depreciation	2008	2007	2006	2008/07	2007/06
YEAR ENDED 30 JUNE	NZ$M	NZ$M	NZ$M	% CHANGE	% CHANGE
New Zealand	453	432	411	4.9	5.1
Australia	114	62	119	83.9	(47.9)
Other	7	6	6	16.7	-
Total depreciation expense	**574**	**500**	**536**	14.8	(6.7)

Depreciation represents a significant component of Telecom's operating expenses, given the major investment in property, plant and equipment required to support its operations.

The level of capital expenditure impacts depreciation expense. Annual capital expenditure is currently in excess of the annual depreciation and this is expected to be the case again in the 2009 financial year. This will ultimately be expected to flow through to higher depreciation charges in future periods.

Depreciation in New Zealand was NZ$453 million in 2008, being a 4.9% increase over 2007 and is attributable to the increased asset base described above, and accelerated depreciation of certain existing assets, such as the CDMA network. Depreciation in Australia was NZ$114 million for 2008, which was NZ$52 million higher than 2007 due to the full-year effect of the PowerTel acquisition.

In 2007 New Zealand depreciation totalled NZ$432 million, an increase of NZ$21 million from 2006 due to the increase in underlying assets. In Australia depreciation was NZ$62 million for 2007. This NZ$57 million decrease from 2006 reflected the lower carrying values arising from the significant impairment recognised in respect of the Australian operations in 2006.

Amortisation	2008	2007	2006	2008/07	2007/06
YEAR ENDED 30 JUNE	NZ$M	NZ$M	NZ$M	% CHANGE	% CHANGE
New Zealand	155	133	112	16.5	18.8
Australia	30	18	50	66.7	(64.0)
Other	2	1	1	100.0	-
Total amortisation expense	**187**	**152**	**163**	23.0	(6.7)

Amortisation expense primarily relates to software assets, spectrum licences and international cable capacity. The expense fluctuates depending on the mix of assets in this category that has increased by NZ$52 million, as detailed in note 15 to the financial statements. The main additions to intangible assets in 2007 and 2008 include Hyperbaric, capacity purchases and software to enable number portability.

Net finance expense

YEAR ENDED 30 JUNE	2008	2007	2006	2008/07	2007/06
	NZ$M	NZ$M	NZ$M	% CHANGE	% CHANGE
Finance income	(119)	(59)	(28)	101.7	110.7
Finance expense	283	300	293	(5.7)	2.4
Interest capitalised	(12)	(11)	(11)	9.1	-
Total net finance expense	**152**	**230**	**254**	(33.9)	(9.4)

Net finance expense decreased across the three-year period due to the investment of the proceeds from the sale of Yellow Pages Group prior to being distributed to shareholders or reinvested in the Telecom group. This is reflected in the finance income increases. Finance expense and interest capitalised have remained broadly constant across the three-year period.

Taxation

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Taxation expense	262	205	351	27.8	(41.6)
Total taxation expense	**262**	**205**	**351**	27.8	(41.6)

The 2008 tax expense was predominantly impacted by Southern Cross dividends that were not subject to New Zealand tax, foreign income being subject to a reduced rate of tax, prior period adjustments and no Australian tax benefit recognised on the current year's results due to their loss-making position. Those impacts result in an effective tax rate for 2008 of 26.9%. The 2007 tax expense was significantly impacted by the recognition of tax benefits arising from a previous write-down of tangible assets included in the impairment charges relating to the group's Australian operations. Excluding this credit, the effective tax rate for 2007 was 29.1%. This was slightly lower than the New Zealand corporate tax rate of 33% due to the non-assessable gain on the sale of Telecom Samoa Cellular Limited, foreign income being subject to a reduced rate of tax and recording the impact of the announced reduction in the New Zealand corporate tax rate.

Segmental results

Telecom's operations consisted of four reportable business segments for the years ending 30 June 2006, 2007 and 2008.

- NZ Business
- NZ Consumer
- NZ Technology and Enterprises
- Australian operations

From 1 July 2008, Telecom reported under the five segments detailed in the Overview section. The financial results for the three-years ended 30 June 2008 are presented under the reportable business segments.

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Segment revenues					
NZ Business	1,811	1,802	1,823	0.5	(1.2)
NZ Consumer	1,611	1,709	1,689	(5.7)	1.2
NZ Technology and Enterprises	493	443	420	11.3	5.5
Australian operations	1,431	1,327	1,323	7.8	0.3
Total segment revenues[1]	**5,346**	**5,281**	**5,255**	1.2	0.5
Segment earnings					
NZ Business	977	1,074	1,123	(9.0)	(4.4)
NZ Consumer	1,024	1,085	1,110	(5.6)	(2.3)
NZ Technology and Enterprises	(847)	(811)	(792)	4.4	2.4
Australian operations	(49)	(51)	(1,386)	(3.9)	NM[1]
Total segment earnings[1]	**1,105**	**1,297**	**55**	(14.8)	NM[1]

1 See note 31 to the financial statements for a reconciliation between segment revenues and consolidated group revenues, and between total segment earnings and consolidated group earnings after income tax. Segment earnings consist of earnings before finance income and finance expense and income tax.

NZ Business

Revenues were stable in NZ Business in 2008 when compared to 2007. Declines, principally due to lower pricing, were experienced in local service, calling and broadband product lines, which were offset by increases in data revenues, growth in IT services and increased demand from Wholesale customers.

Segment earnings for NZ Business declined in 2008 by NZ$97 million when compared to 2007 due to the mix of sales from traditionally higher margin products, such as calling products, to lower margin products, such as IT services. These factors also impacted the 2007 results which declined by NZ$49 million when compared to 2006.

Revenues declined in NZ Business in 2007 when compared to 2006 through the erosion of traditional voice revenues and the impacts of broadband pricing. Local calling revenues declined as chargeable minute volumes declined while average prices remained stable. Data revenues also declined, as noted above, driven by a decrease in traditional data services, partially offset by increased managed IP data services.

Earnings declined in 2007 when compared to 2006, impacted by the change in the mix of sales from traditionally higher margin products, such as calling products, to lower margin products, such as IT services.

NZ Consumer

NZ Consumer revenues decreased in 2008 when compared to 2007 due to pricing and volume declines in local, calling, mobile and dial-up internet revenues, partially offset by the growth in broadband.

The 2008 earnings from NZ Consumer declined from 2007 by NZ$61 million to NZ$1,024 million due to the effects of lower overall pricing and lower demand for dial-up internet, which was partially offset by the effects of higher broadband revenues and lower mobile direct costs, due to lower demand for mobiles. Earnings decreased by NZ$25 million in 2007 as compared to 2006 as customer numbers continued to increase offset by the impact of acquisition and retention of mobile customers continuing to increase direct costs of sales with subsidies on mobile handsets and increased retention costs.

NZ Consumer revenues increased in 2007 as compared with 2006 as growth in mobile revenues, driven by increased text messaging volumes resulting from growth in the customer base, and broadband increased while traditional revenues declined due to competition in the market and due to fixed to mobile substitution. Calling revenues declined as the average price of a calling minute declined across all products and volumes of calling minutes declined across most products except calls to mobile phones and increased penetration of high-speed mobile data services.

Earnings decreased in 2007 compared to 2006 as customer numbers continued to increase, offset by the impact of acquisition and retention of mobile customers continuing to increase direct costs of sales with subsidies on mobile handsets and increased retention costs. Broadband continued to grow in connections numbers and despite a fall in the average broadband revenue per connection, the growth in broadband revenues exceeded the decline in dial-up internet revenues.

NZ Technology and Enterprises

NZ Technology and Enterprises contains the costs of the maintenance of the New Zealand networks, wholesale services and the provision of shared financial services for the Telecom group. As these costs related to the revenue-generating activities of other segments, NZ Technology and Enterprises is a loss-making segment and would not normally generate a profit from its ordinary operations. Revenues consist principally of wholesale revenues. These revenues increased by 11.3% in 2008 when compared to 2007 and 5.5% in 2007 when compared to 2006 due to increased demand from wholesale customers. Costs include the majority of depreciation and amortisation and staff costs. Movements in these costs are discussed above in relation to total New Zealand costs. The increases are due to the factors discussed above that relate to increasing levels of capital expenditure driving higher depreciation and amortisation, the provisioning of broadband driving higher direct costs and the costs of maintaining the network.

Australian operations

Reported NZ$ results from Telecom's Australian operations have been impacted by movements in exchange rates. The average NZ$:A$ exchange rates for 2008, 2007 and 2006 are shown in the table below.

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Average NZ$/A$ exchange rate	0.8577	0.8717	0.8949	(1.6)	(2.6)

The average exchange rate for 2008 and 2007 is lower than the average exchange rate for the previous year, resulting in an equivalent increase in reported NZ$ revenues, expenses and loss for Australian operations.

Following the purchase of PowerTel in May 2007 the Australian results include the consolidated results of AAPT and PowerTel, hence year-on-year results are not comparable. AAPT and PowerTel commenced integration in 2007 therefore separate results are not available for 2008.

In 2008 revenue increased from 2007 by NZ$104 million to NZ$1,431 million, due to the effects of PowerTel as well as increases in wholesale and data revenues. These increases were partially offset by declining revenues from traditional service lines such as local service, calling and mobile due to lower pricing and lower consumer customer numbers. A stand alone mobile customer base was also disposed of at the beginning of 2008.

Australian Operations have continued to be negatively impacted by tightening of wholesale prices and intense competition in the Australian market by its competitors. These factors contributed to the Australian Operations being loss-making. Australian Operations earnings were also impacted in 2008 by staffing call centres due to high call volume as a result of a new billing platform and the additional costs incurred to rectify these issues.

Included in the results of Australian operations for 2007 was NZ$43 million of revenue and NZ$2 million loss for the period from 9 May 2007 to 30 June 2007 relating to PowerTel.

Excluding the impact of PowerTel, total revenue decreased principally due to declining revenue from national calls, partially offset by growth in resale revenue. Revenue from national calls decreased due to competitive pressure and capped calling plans driving a lower average price per minute for 2007. The churn of large corporate customers has also impacted the volume of calls. International calling revenue decreased due to both a decrease in volumes and a decrease in average price per minute.
The active consumer fixed line customer base decreased during 2007 due to the decision to terminate the high churning external sales channels in October 2006 and focus on churn management.

Included in segment earnings for 2006 were impairment write-downs totalling NZ$1,301 million. These reflected adverse trends impacting the short and long-term earnings outlook for Australian operations, particularly:

- A significant tightening of wholesale prices and terms with Telstra (the principal supplier to Telecom's Australian operations)
- Sustained downward pressure on retail prices
- The deferral of major project expenditure by key corporate customers.

As well as leading to the impairment charge, these factors also had a significant negative impact on results for Australian operations in 2006. Excluding the impairment charge, segment earnings for 2006 were a loss of NZ$85 million.

Critical accounting policies and recently issued accounting standards

See note 1 to the financial statements for Telecom's critical accounting policies.

See note 37 to the financial statements for the potential impact of recently issued accounting standards.

Dividend policy and long-term capital management

Liquidity and capital resources

Telecom's principal sources of liquidity are operating cash flows and external borrowing from established debt programmes and bank facilities. In addition to these principal sources of liquidity Telecom received NZ$2,161 million for the sale of its Yellow Pages Group in 2007. NZ$1,113 million of the NZ$2,161 million that Telecom received from the sale was returned to shareholders in October 2007 as part of a capital return by way of a court-approved pro-rata share cancellation, which involved the cancellation of one in nine ordinary shares on a pro-rata basis in exchange for NZ$4.88 for each cancelled share. With regards to American Depositary Receipts ('ADR') holders, following the capital return the ratio of ADR to ordinary shares was changed from 1 ADR to 8 ordinary shares to 1 ADR to 5 ordinary shares. From an ADR holder's perspective the combination of the capital return and ratio change resulted in the receipt of approximately US$3.27 for every existing ADR held and the issue of 42.2% more ADRs.

The Telecom board continues to be committed to Telecom maintaining 'single A' credit ratings from Moody's Investors Service and Standard & Poor's and its capital management policies are designed to ensure this objective is met. Relevant factors include Telecom's debt profile, operating outlook, cash flow and cost of capital. As a guide, Telecom expects to maintain a relatively stable capital structure with the intention that, in normal circumstances, the ratio of net debt to EBITDA would not materially exceed 1.7 times on a long-run basis. The extent of funds available to pay dividends is driven by the level of earnings as well as future capital expenditure requirements and investment needs.

Cash flows

The following table sets out information regarding Telecom's cash flows during the three-year period:

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Net cash from					
Operating activities[1]	1,685	1,651	1,807	2.1	(8.6)
Investing activities[1]	(890)	1,028	(453)	NM[2]	NM[2]
Financing activities[1]	(2,036)	(852)	(1,434)	139.0	(40.6)
Foreign exchange movement	51	(13)	-	NM[2]	NM[2]
Net (decrease)/increase in cash	**(1,190)**	**1,814**	**(80)**	NM[2]	NM[2]

1 See cash flow note in financial statements for breakdown

2 Not meaningful.

Net cash from operating activities

Net cash flows from operating activities increased by NZ$34 million in 2008. Cash payments to suppliers and employees increased by NZ$33 million due to timing differences, and there was a decrease in cash received from customers of NZ$143 million due to declining revenues. Cash received from interest income increased by NZ$74 million as a result of the investment of the proceeds from the sale of Yellow Pages Group. Dividends of NZ$89 million were received from Southern Cross.

Net cash flows from operating activities decreased by 8.6% in 2007 compared to 2006. This was principally due to an increase in payments made to suppliers and employees that increased by 6.4%. This increase was as a result of increased labour expenses and operating expenses and an unfavourable movement in working capital experienced towards the end of 2007. Offsetting this increase in cash outflows was an increase in interest income received due to higher cash on deposit, dividends received from Southern Cross and lower income tax and interest payments.

Net cash from investing activities

Net cash from investing activities decreased by NZ$1,918 million in 2008. The decrease is principally a result of 2007 including the cash inflow from the sale of Yellow Pages Group and the repayment of the advance to Southern Cross, adjusted for the acquisition of PowerTel. Investing activities include the expenditure on the purchase of property, plant and equipment, and intangible assets (capital expenditure) that is presented in the table below.

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
New Zealand	832	637	592	30.6	7.6
Australia	112	147	131	(23.8)	12.2
Corporate and other	43	48	17	(10.4)	182.4
Total capital expenditure[1]	**987**	**832**	**740**	**18.6**	**12.4**

1 Capital expenditure is measured on an accruals rather a cash basis.

In 2008 New Zealand capital expenditure comprised of:

- NZ$219 million (2007: NZ$187 million) related to investment needed to meet statutory, regulatory and contractual obligations and to sustain existing service performance
- NZ$97 million (2007: NZ$62 million) related to the investment in the technology and services required to deliver NGT
- NZ$359 million (2007: NZ$213 million) related to investment required to extend network coverage, augment capacity in line with strategic business growth (eg, growth in broadband and mobile), develop and deploy new technology capabilities needed to deliver retail and wholesale services cost-effectively, and to implement the requirements of the Telecommunications Act 2006 and Telecom's Undertakings
- NZ$54 million (2007: NZ$87 million) was investment in service-specific and customer service systems needed to deliver, grow and sustain retail services
- NZ$103 million (2007: NZ$88 million) comprised investment outside the core strategic programmes that is justified based on the projected rate of return of the investment.

The main increases in expenditure related to the expenditure on the NGN to build VoIP capability, create infrastructure for new channel capability (particularly online), develop new customer management systems and establish new technology management capability. Other areas of increase included expenditure on ICT outsourcing and customer premises equipment investment, developing contact centre and customer service systems and capability and the acquisition of international network capacity.

In 2008 capital expenditure in Australia amounted to NZ$112 million. This decreased by NZ$35 million compared to 2007 due to the completion of the Hyperbaric project. In 2007, capital expenditure of NZ$147 million increased by NZ$16 million (12.2%) compared to 2006. Expenditure for 2007 included the final phase of expenditure on call centre functionality and IT platforms and the move away from networks to 'enabling' infrastructure.

For 2009 Telecom currently expects that capital expenditure will be up to NZ$1,100 million as Telecom delivers on its transformation strategies. This is principally due to the expected expenditure on the WCDMA network, spending on next generation capability and the fibre network rollout. It is expected that this expenditure will be financed from operating cash flows, existing cash reserves and new debt that has been raised after 30 June 2008 (see note 22 of the financial statements).

Management believes Telecom's net cash flows generated from operations and its existing available cash and borrowings will be sufficient to fund Telecom's expected capital expenditure, working capital and investment requirements for 2009. Management also considers that Telecom is in a satisfactory position to meet its longer term cash requirements. Telecom has a satisfactory spread of debt maturities, with maturities extending up to 12 years for its longest dated debt issues. Telecom has access to sufficient borrowing capacity to meet its needs and in the event that operating cash flows declined to levels that are materially lower than those being generated at present, Telecom could respond by reducing dividend payments and/or capital expenditure.

Net cash flow from financing activities

Cash flows for financing activities largely reflect borrowing activities and dividend payments to shareholders.

In 2008 net cash flow from financing activities increased by NZ$1,184 million compared to 2007 principally due to the capital return of NZ$1,113 million, which occurred in October 2007. Removing the impact of the capital return, net cash outflow from financing activities was NZ$923 million, an increase of NZ$71 million principally due to an increase in dividends paid of NZ$68 million.

The net cash flow from financing activities decreased by NZ$582 million for 2007 compared to 2006. The decrease was primarily due to a decrease in the dividend paid, as the prior period included the payment of special dividends declared in respect of the 2005 financial year. There were no repurchases of shares in connection with the dividend reinvestment plan in 2007, which also reduced the cash outflow from financing activities.

Working capital

Telecom defines its working capital as the difference between current assets and current liabilities. Telecom's working capital position is shown in the table below:

YEAR ENDED 30 JUNE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008/07 % CHANGE	2007/06 % CHANGE
Current assets	1,856	3,079	1,325	(39.7)	132.4
Current liabilities	(2,280)	(1,590)	(2,119)	43.4	(25.0)
(Deficit)/surplus in working capital	**(424)**	**1,489**	**(794)**	NM[1]	NM[1]

1 Not meaningful.

As at 30 June 2008, Telecom's current liabilities exceed current assets. Telecom has positive operating cash flows that enable working capital to be managed to meet short-term liabilities as they fall due. The increase in current liabilities in 2008 from 2007 is due to an increase in debt due within one year.

The decrease in current assets in 2008 is due to the reversal of the increase in current assets in 2007 that was due to the receipt of the sales proceeds from the sale of Yellow Pages Group. NZ$1,113 million of this amount was returned to shareholders in October 2007.

As detailed in note 22 to the financial statements, Telecom raised NZ$142 million of Telebonds and NZ$258 million of Euro Medium Term Notes in July and August 2008, and Telecom has stand-by facilities in excess of NZ$800 million.

As at 30 June 2008 the consolidated net tangible assets per share was NZ$0.96 (30 June 2007: $1.33). Net tangible assets per share is a non-GAAP financial measure and is not prepared in accordance with NZ IFRS. It is required to be disclosed by New Zealand stock exchange listing requirements. The calculation of Telecom's consolidated net tangible assets and its reconciliation to the consolidated balance sheet is presented below:

AS AT 30 JUNE	2008	2007
Total assets (NZ$m)	7,405	8,276
Less intangible assets (NZ$m)	(990)	(927)
Less total liabilities (NZ$m)	(4,669)	(4,672)
Net tangible assets (NZ$m)	1,746	2,677
Number of shares outstanding (m)	1,826	2,020
Net tangible assets per share (NZ$/share)	**0.96**	**1.33**

Credit ratings

In June 2008 Telecom's long-term credit ratings were a Standard & Poor's rating of A (outlook stable) and a Moody's Investors Service's rating of A2 (outlook negative). Ratings are not a recommendation to purchase, hold or sell securities, and may be changed, superseded or withdrawn at any time.

Funding Sources and Requirements

Telecom's funding sources, level of borrowings and maturity profile are detailed in note 26 to the financial statements.

Telecom's future borrowing requirements are dependent on revenue receipts, capital expenditure requirements, distributions to shareholders, taxation payments, servicing and repayment of existing debt and other business requirements as determined from time to time. There is no particular seasonality to borrowing requirements.

Cash requirements and commitments

Telecom's contractual obligations and other commercial commitments as at 30 June 2008 are set out in the table below.

		PAYMENTS DUE BY PERIOD			
	TOTAL	LESS THAN 1 YEAR	1-3 YEARS	4-5 YEARS	AFTER 5 YEARS
Contractual obligations	NZ$M	NZ$M	NZ$M	NZ$M	NZ$M
Short-term debt	406	406	-	-	-
Long-term debt	2,400	559	29	582	1,230
Derivative liabilities	1,074	293	164	388	229
Operating leases	493	73	133	73	214
Capital expenditure	259	259	-	-	-
Interest payments on term debt[1]	847	144	218	195	290
Operating expenditure commitments	20	20	-	-	-
Total contractual cash obligations	**5,499**	**1,754**	**544**	**1,238**	**1,963**

Other commercial commitments		AMOUNT OF COMMITMENT EXPIRATION BY PERIOD			
	TOTAL COMMITTED	LESS THAN 1 YEAR	1-3 YEARS	4-5 YEARS	AFTER 5 YEARS
	NZ$M	NZ$M	NZ$M	NZ$M	NZ$M
Guarantees[2]	277	31	106	53	87

1 Future interest payments on the portion of term debt subject to floating interest rates are calculated based on current interest rates.

2 Guarantees principally consist of cross border lease guarantees in respect of certain telecommunications asset sale and leaseback transactions. Telecom has given certain undertakings in accordance with limited guarantees entered into as part of the transactions. The amount disclosed above is the maximum exposure under the guarantees, however, Telecom believes that the likelihood of losses in respect of these matters is remote.

Off-balance sheet arrangements

Telecom does not have any off-balance sheet arrangements, as the term is defined for the purposes of Item 5.E of the Form 20-F, that have or are reasonably likely to have a current or future effect on Telecom's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that are material to investors.

Treasury and interest rate management

Telecom manages its treasury activities through a board-approved treasury constitution consisting of treasury governance and policy frameworks. Telecom is exposed to foreign currency fluctuations through borrowing in foreign currencies, making capital and operating expenditure purchases in foreign currencies and operating in the wholesale international telecommunications market, as well as through the impact that foreign currency fluctuations have on reported results of foreign subsidiaries.

Telecom generally funds all or a portion of its significant offshore investments in the currency of the investment. AAPT and PowerTel are funded in Australian dollars. Other than these borrowings that remain in foreign currencies and are matched against foreign denominated assets, foreign currency borrowings are hedged at inception into NZ dollars using cross currency interest rate swaps. Telecom also hedges a portion of its foreign currency purchases forecast for the next 12 months and hedges the net balance sheet position of its international operations. The objectives of interest rate risk management are to minimise the cost of net borrowings and to minimise the impact of interest rate movements on Telecom's interest expense and net earnings within policies approved by Telecom's board.

For further details of Telecom's exposure to interest rate risk, foreign currency risk and its related use of derivatives see note 26 to the financial statements.

Below is certain information concerning exchange rates between NZ dollars and US dollars (expressed in US dollars per NZ$1.00) based on the noon buying rate in New York City for cable transfers in NZ dollars as reported by the Federal Reserve Bank of New York (Exchange Rate).

On 11 August 2008 the Exchange Rate was 0.7010.

The high and low exchange rates for each month during the previous six months were as follows:

Month	High	Low
February 2008	0.8124	0.7784
March 2008	0.8213	0.7847
April 2008	0.8035	0.7728
May 2008	0.7938	0.7536
June 2008	0.7894	0.7447
July 2008	0.7762	0.7316

The average exchange rates, determined by averaging the exchange rates on the last day of each month during the year for the financial periods specified below were as follows:

YEAR ENDED 30 JUNE	Average
2004	0.6304
2005	0.6980
2006	0.6673
2007	0.6921
2008	0.7705

Dividend policy

Based on Telecom's current expectations for the next twelve months, the target dividend payout for 2009 will be to pay out the higher of 75% of net earnings (after adding back relevant non-cash items) or quarterly dividends of 6 cents per share, subject to there being no material adverse change in circumstances.

The dividend reinvestment plan has been retained. Shares issued under the plan are priced at the prevailing market price and Telecom intends to acquire an equivalent number of shares on-market, in order to eliminate an increase in capital arising pursuant to the plan. These mechanisms are reviewed at each dividend date.

Controls and procedures

Telecom's management, with the participation of Telecom's Chief Executive Officer and Telecom's Chief Financial Officer, evaluated the effectiveness of Telecom's disclosure controls and procedures as of 30 June 2008. In designing and evaluating the disclosure controls and procedures, management recognised that any controls and procedures, no matter how well designed and operated, can provide only reasonable, rather than absolute, assurance of achieving the desired control objectives, and management necessarily was required to apply its judgement in evaluating the cost-benefit relationship of possible controls and procedures.

Based upon that evaluation and taking into account the foregoing, Telecom's Chief Executive Officer and Telecom's Chief Financial Officer concluded that, as of 30 June 2008, Telecom's disclosure controls and procedures are effective in providing reasonable assurance that information required to be disclosed by Telecom in the reports that it files or submits under the United States Securities Exchange Act is recorded, processed, summarised and reported on a timely basis, and are effective in ensuring that information required to be disclosed by Telecom in the reports it files or submits under the United States Securities Exchange Act is accumulated and communicated to Telecom's management, including its principal financial and executive officers, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure.

Management's report on internal control over financial reporting

Telecom's management is responsible for establishing and maintaining adequate internal control over financial reporting. Telecom's internal control over financial reporting is designed

to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes.

Under the supervision and with the participation of Telecom's Chief Executive Officer and Telecom's Chief Financial Officer, Telecom's management evaluated the effectiveness of Telecom's internal control over financial reporting as of 30 June 2008 based upon the framework in 'Internal Control – Integrated Framework' issued by the Committee of Sponsoring Organizations of the Treadway Commission.

Based upon that evaluation, Telecom's management has concluded that, as of 30 June 2008, Telecom's internal control over financial reporting is effective.

KPMG, Telecom's independent registered public accounting firm, has audited the consolidated financial statements included in this annual report and, as a part of the audit, has reported on the effectiveness of Telecom's internal control over financial reporting.

Changes in internal control over financial reporting

There have been no changes in Telecom's internal control over financial reporting during the year ended 30 June 2008 that have materially affected, or are reasonably likely to materially affect, Telecom's internal control over financial reporting, which report is on page 64.

Group risk factors

Operational separation could have a greater adverse effect on Telecom's businesses, results of operations, financial condition and prospects than currently being experienced

Compliance with the Undertakings has led to the restructure of Telecom's business units, including the launch of Chorus, Telecom's separate access network business unit, requiring Telecom to re-engineer systems and processes and accommodate significant behavioural changes in the process. To date, operational separation has involved significant establishment costs, and Telecom expects that it will necessitate increased ongoing costs.

Operational separation could also result in a decline in operational effectiveness due to increased administrative processes, duplication of roles and activities across the separated parts of the business, loss of the ability to access the benefits of a vertically integrated organisation, and reduced speed-to-market. The implementation of operational separation also requires significant attention from Telecom's management, diverting their focus from transformational and other business improvement initiatives.

In the longer term, Telecom may fail to deliver required milestones, or breach the required behavioural conduct, leading to fines, reputational damage and potentially additional industry regulation.

Telecom may be unable to contain its capital spend or may experience an opportunity cost associated with capital control

Telecom's business is capital intensive and significant investment in technology and other assets is required before new services can be released to the market. In the 2008 and 2007 financial years, Telecom invested NZ$987 million and NZ$844 million, respectively, in capital expenditure principally on telecommunications and network equipment.

In order to implement its strategy, Telecom has forecasted capital expenditure of up to NZ$1,100 million in 2009 to:

- Continue implementation of a next generation network to replace legacy PSTN service platforms
- Develop operational support systems to complement new business models
- Continue to grow broadband and mobile market share.

However, competitive or regulatory drivers may accelerate the need for capital expenditure in these key areas. Additionally, the ability to contain capital spend is under continual pressure from the increased complexity inherent in the delivery of new and emerging technologies in response to market changes. For example, if Telecom were to rollout 3G WCDMA nationally at 850MHz in New Zealand, its capital expenditure requirements in the short term would increase. These factors may also lead to Telecom being required to invest in new technologies earlier than originally planned.

Accordingly, Telecom's capital spend may exceed current market and management expectations, negatively impacting Telecom's return on investment, future profitability and its ability to raise future capital funds on acceptable terms.

Capital constraints may impede Telecom's ability to pursue growth investment opportunities in key areas such as mobile, broadband, IT solutions and 'new wave' products. Should this occur, Telecom's ability to maintain competitive positioning and grow its future revenues may be impacted.

Telecom may not succeed in targeting growth in mobile, broadband and ICT capability

Telecom's strategy for transformation includes the targeting of growth in mobile, broadband and ICT capability.

Telecom may be unable to execute its strategy of targeting growth in the mobile market due to a combination of factors, including:

- Uncertain mobile market regulatory outcomes, whereby mobile services that are largely unregulated at present, may be subject to regulation in the future
- New competition entering the New Zealand mobile market that may cause prices for mobile telecommunications services to decline
- The loss of mobile customers using Telecom's CDMA network due to reduced handset and device availability that is likely to arise as a result of the declining global market share for CDMA

- Possible delays to commission Telecom's WCDMA network and a potential inability to successfully leverage benefits from delivery of the new network
- Legacy infrastructure may limit Telecom's ability to match competitor offerings.

Telecom's retail business may fail to achieve a competitive broadband proposition due to a combination of factors such as competition for resources with other business units, reduced customer broadband spend, operational separation requirements requiring inefficient or ineffective process redesign, and a negative perception of Telecom due to prior performance issues associated with the Yahoo!Xtra migration.

Gen-i's ability to grow market share, customer preference and margin in the ICT market may be impacted by factors such as its ability to deliver a quality end-to-end service, increased competition in the ICT space from existing competitors, and new competition from IT integrators and other Telecom business units.

In view of the likely level of competition and uncertainties regarding the level of economic activity, there can be no certainty that Telecom will meet its growth targets in mobile, broadband and ICT, with a consequential impact on future revenue and profitability.

Telecom may not succeed in implementing its NGT business model and NGN. Even if successfully implemented, Telecom may be unable to deliver sustainable cash flows from its new business models

To improve its financial results and offset the impact of margin declines in its traditional communications business, Telecom is implementing a transformation strategy that requires substantial investment in large scale replacement of its network, IT and other technical infrastructure and moving to a lower cost IP model. Telecom has set an aggressive timeframe for implementing its next generation Telecom (NGT) business model, and its supporting IP-based next generation network (NGN), over the period to 2012.

Telecom faces a number of risks in the delivery of the expected cost savings and other benefits expected from its NGT and NGN. These include:

- Telecom's next generation technologies and network, and IT support systems and processes may not function as anticipated
- Key vendors and other partners may not perform as expected
- Customer take-up of and planned large-scale migration to Telecom's new products and services may be significantly less than planned
- Extended delays and other execution problems in implementing Telecom's transformation strategy may develop
- Competitors may offer similar services and capabilities
- Possibility of future regulation providing industry access to Telecom's next generation investments.

In the event business transformation initiatives fail to deliver the expected cost, revenue and new functionality upsides, Telecom's competitive capability and ability to generate earnings may reduce over time.

Telecom's wholesale business faces increasing competition

The performance of Telecom's wholesale business may be adversely affected by competitive forces in the markets in which it operates, such as competition from alternative network providers reducing market share and causing price erosion in its data markets. Also, the successful take-up of Chorus' UCLL product may significantly affect Wholesale's resale product portfolio. Chorus customers purchasing UCLL may be able to acquire the end-user customers of Wholesale's customers (other service providers) reducing demand for Wholesale products and services. Depending on the size and speed of competitive investment in UCLL, Wholesale's revenues may be adversely affected.

Network and system failures could damage Telecom's reputation and earnings

Telecom's network infrastructure (including exchanges), particularly in New Zealand, is geographically widespread and is vulnerable to natural disasters.

Increased failure rates and increasing difficulty supporting ageing legacy technologies, in combination with potentially reduced reliability of new IP-based technologies, may prevent Telecom servicing customers and/or cause increased loss from service events.

Many internal and network systems are crucial to supporting Telecom's ability to provide reliable, uninterrupted customer service. Some of these systems are approaching the end of their useful lives and may not be replaced, upgraded or phased out before problems of capacity, spares, supplier support and increased fault levels occur. While there are initiatives in place to manage these systems the risk of a significant systems or exchange outage resulting in an adverse impact on customers remains high.

A serious service failure could adversely impact financial performance, and company reputation and may attract additional industry regulation.

Telecom may be unable to reduce legacy costs

Telecom's ability to reduce legacy costs in order to improve profitability may be impaired by a combination of factors, such as increased operating costs arising from operational separation, delays in the availability of new technology and new products and services, asset write-downs, price increases for key services such as network maintenance, and major contract re-negotiations with key network suppliers.

Collectively, these factors may prevent Telecom from achieving its planned levels of legacy cost reductions, placing pressure on its ongoing levels of profitability and cash flows.

Telecom faces increased dependence on its outsourced suppliers

Telecom is increasingly dependent upon key technology partners for the supply, operation and in some cases, the design, of its network and IT infrastructure and associated business support platforms. Additionally, outsourcing and business partners occupy a key role in the delivery of future transformation and regulatory programmes.

Failure by Telecom's key partners to supply equipment, services or required deliverables within acceptable cost, time and quality requirements could affect Telecom's financial position and performance.

Telecom's Australian businesses may be unable to improve their financial performance

Achieving profitable operations in AAPT and Gen-i in Australia is dependent on a combination of factors such as successfully executing business transformation initiatives, delivering a compelling, high quality customer service experience and building scale through the acquisition and retention of high value customers.

In the event that Telecom's Australian businesses are unable to successfully execute these strategies, a return to profitable Australian operations may be prevented, impairing the returns available from Telecom's Australian investments, and reducing Telecom's overall profitability.

Future changes to the New Zealand regulatory environment

Despite the recent widespread regulatory reforms, potential exists for further regulation that may have an adverse effect on Telecom's New Zealand operations and ongoing profitability.

Areas for which studies are currently under way that may be subject to further regulatory or legislative change include the Telecommunications Service Obligation, rural broadband, the review of the numbering arrangements in New Zealand and 'Next Generation' technical and service infrastructures and mobility.

In the event further industry-related regulation occurs, there is potential for these changes to be less advantageous than those Telecom currently operates under. This could increase the costs of Telecom's operations, or reduce its ability to generate future revenues.

Telecom could experience difficulty in retaining and attracting skilled and experienced people

As technology evolves, Telecom will need to attract, retain and train its workforce. The relevant skills are in short supply worldwide. There is a risk that an inability to attract and retain skilled and experienced people and hence to embrace new technology could impact Telecom's ability to remain competitive.

The demand for Telecom's services is influenced by economic conditions

Telecom's business is influenced by economic conditions within the countries in which it operates, and in particular by the state of the New Zealand and Australian economies and also the economies of their major trading partners. A significant weakening in the New Zealand or Australian economy could have a material adverse effect on Telecom's business and results of operations.

A change in the assumptions that support the carrying value of Telecom's goodwill and investments may lead to future impairment

As at 30 June 2008, Telecom had NZ$697 million of goodwill and long-term investments. Telecom assesses the carrying value of its goodwill and investments on a regular basis. As detailed in critical accounting policies in note 1 to the financial statements, this assessment is based on a number of assumptions, including expected rate of growth of revenues, margins expected to be achieved, the level of future capital expenditure required to support these outcomes and the appropriate discount rate to apply when valuing future cash flows.

Any future adverse impacts arising in assessing the carrying value of Telecom's goodwill and investments could lead to future impairment that would affect future earnings.

Auditors' reports

New Zealand Opinion

To the shareholders of Telecom Corporation of New Zealand Limited

We have audited the financial statements that consist of the income statement, the statement of changes in equity, the balance sheet, the cash flow statement and Notes 1 to 37. The financial statements provide information about the past financial performance and financial position of the company and group as at 30 June 2008. This information is stated in accordance with the accounting policies set out in Note 1 to the financial statements.

Directors' responsibilities

The Directors are responsible for the preparation of financial statements which give a true and fair view of the financial position of the company and group as at 30 June 2008 and the results of their operations and cash flows for the year ended on that date.

Auditors' responsibilities

It is our responsibility to express an independent opinion on the financial statements presented by the Directors and report our opinion to you.

Basis of opinion

An audit includes examining, on a test basis, evidence relevant to the amounts and disclosures in the financial statements. It also includes assessing:

- the significant estimates and judgements made by the Directors in the preparation of the financial statements;
- whether the accounting policies are appropriate to the company's and group's circumstances, consistently applied and adequately disclosed.

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

Other than in our capacity as auditors we have no relationship with or interests in the company. Partners and employees of our firm may also deal with the company and group on normal terms within the ordinary course of trading activities of the business of the company and group. These matters have not impaired our independence as auditors of the company and group.

Unqualified opinion

We have obtained all the information and explanations we have required.

In our opinion:

- proper accounting records have been kept by the company as far as appears from our examination of those records;
- the financial statements:
  - comply with International Financial Reporting Standards as issued by the International Accounting Standards Board;
  - comply with New Zealand generally accepted accounting practice;
  - give a true and fair view of the financial position of the company and group as at 30 June 2008 and the results of their operations and cash flows for the year ended on that date.

Our audit was completed on 21 August 2008 and our unqualified opinion is expressed as at that date.

KPMG

Wellington, New Zealand

21 August 2008

United States Opinion

Report of Independent Registered Public Accounting Firm

The Board of Directors and Shareholders of Telecom Corporation of New Zealand Limited

We have audited the accompanying consolidated balance sheets of Telecom Corporation of New Zealand Limited and subsidiaries (the Group) as of 30 June 2008 and 2007, and the related consolidated income statements, statements of changes in equity, and cash flow statements for each of the years in the three-year period ended 30 June 2008. We also have audited the Group's internal control over financial reporting as of 30 June 2008, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. The Group's management is responsible for these consolidated financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements and an opinion on the Group's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the consolidated financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorisations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorised acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Group as of 30 June 2008 and 2007, and the results of its operations and its cash flows for each of the years in the three-year period ended 30 June 2008, in conformity with International Financial Reporting Standards as issued by the International Accounting Standards Board. Also in our opinion, the Group maintained, in all material respects, effective internal control over financial reporting as of 30 June 2008, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission.

KPMG

Wellington, New Zealand

21 August 2008

PERFORMANCE

Financial statements

Income statements

For the years ended 30 June 2008, 2007 and 2006

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS)	NOTES	GROUP 2008 NZ$M	GROUP 2007 NZ$M	GROUP 2006 NZ$M	PARENT 2008 NZ$M	PARENT 2007 NZ$M
Operating revenues and other gains	2					
Local service		1,129	1,084	1,081	-	-
Calling	3	1,233	1,336	1,385	-	-
Interconnection		178	187	201	-	-
Mobile		833	895	869	-	-
Data		638	561	602	-	-
Broadband and internet		547	485	448	-	-
IT services		439	380	346	-	-
Other operating revenues	3	669	634	563	544	3,347
Other gains	5	7	20	60	-	-
		5,673	**5,582**	**5,555**	**544**	**3,347**
Operating expenses	4					
Labour		(886)	(773)	(760)	-	-
Intercarrier costs		(1,243)	(1,220)	(1,199)	-	-
Other operating expenses		(1,653)	(1,603)	(1,497)	-	-
Asset impairments	5	-	-	(1,301)	-	-
Other expenses	5	-	(52)	(34)	(423)	(638)
Depreciation		(574)	(500)	(536)	-	-
Amortisation		(187)	(152)	(163)	-	-
		(4,543)	**(4,300)**	**(5,490)**	**(423)**	**(638)**
Finance income	6	119	59	28	311	317
Finance expense	6	(271)	(289)	(282)	(432)	(396)
Share of associates' net losses		(3)	(3)	-	-	-
		(155)	**(233)**	**(254)**	**(121)**	**(79)**
Net earnings/(loss) before income tax		**975**	**1,049**	**(189)**	**-**	**2,630**
Income tax (expense)/credit	7	(262)	(205)	(351)	40	26
Net earnings/(loss) from continuing operations		**713**	**844**	**(540)**	**40**	**2,656**
Net earnings from discontinued operation (net of tax)	36	-	2,183	109	-	-
Net earnings/(loss) for the year		**713**	**3,027**	**(431)**	**40**	**2,656**
Net earnings/(loss) for the year is attributable to:						
Equity holders of the company		710	3,024	(435)	40	2,656
Minority interests		3	3	4	-	-
Basic net earnings/(loss) per share (in dollars)	23	NZ$0.38	NZ$1.52	NZ$(0.22)		
Diluted net earnings/(loss) per share (in dollars)	23	NZ$0.38	NZ$1.50	NZ$(0.22)		
Basic earnings/(loss) per share from continuing operations (in dollars)	23	NZ$0.38	NZ$0.42	NZ$(0.28)		
Diluted earnings/(loss) per share from continuing operations (in dollars)	23	NZ$0.38	NZ$0.42	NZ$(0.28)		
Basic earnings per share from discontinued operations (in dollars)	23	-	NZ$1.10	NZ$0.06		
Diluted earnings per share from discontinued operations (in dollars)	23	-	NZ$1.08	NZ$0.06		
Weighted average number of ordinary shares outstanding (in millions)		1,871	1,990	1,960		

See accompanying notes to the financial statements.

Statement of changes in equity

For the years ended 30 June 2008, 2007 and 2006

YEAR ENDED 30 JUNE		GROUP			PARENT	
(DOLLARS IN MILLIONS)	NOTE	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008 NZ$M	2007 NZ$M
Balance at beginning of year		**3,604**	**1,062**	**2,430**	**2,933**	**679**
Translation of foreign operations		103	(120)	176	-	-
Hedge of net investment		(70)	38	(87)	-	-
Revaluation of listed investments		(11)	11	-	-	-
Cash flow hedges		51	(8)	5	-	-
Total (loss)/income recognised directly in equity		73	(79)	94	-	-
Net earnings/(loss) for the year		713	3,027	(431)	40	2,656
Total recognised income and expenses		786	2,948	(337)	40	2,656
Dividends		(762)	(739)	(1,184)	(760)	(735)
Tax credit on supplementary dividends		85	83	131	85	83
Dividend reinvestment plan		195	249	114	195	249
Exercise of share options		-	1	18	-	1
Issuance of shares under employee share schemes		6	-	4	6	-
Capital reduction		(1,113)	-	-	(1,113)	-
Repurchase of shares		(65)	-	(114)	(65)	-
Balance at end of year	23	**2,736**	**3,604**	**1,062**	**1,321**	**2,933**
Total recognised income and expenses for the year is attributable to:						
Equity holders of the company		783	2,945	(341)	40	2,656
Minority interests	23	3	3	4	-	-
Total recognised income and expenses		**786**	**2,948**	**(337)**	**40**	**2,656**

See accompanying notes to the financial statements.

Balance sheets

As at 30 June 2008 and 2007

		GROUP		PARENT	
AS AT 30 JUNE		2008	2007	2008	2007
(DOLLARS IN MILLIONS)	NOTES	NZ$M	NZ$M	NZ$M	NZ$M
ASSETS					
Current assets:					
Cash		779	1,969	-	-
Short-term investments	8	-	70	-	-
Short-term derivative assets	9	15	8	-	-
Receivables and prepayments	10	912	953	689	795
Taxation recoverable		93	8	-	-
Inventories	11	57	71	-	-
Total current assets		1,856	3,079	689	795
Non-current assets:					
Long-term investments	12	527	494	9,262	9,591
Deferred tax assets	13	-	27	-	-
Long-term derivative assets	14	48	68	-	-
Intangible assets	15	990	927	-	-
Property, plant and equipment	16	3,984	3,681	-	-
Total non-current assets		5,549	5,197	9,262	9,591
Total assets		**7,405**	**8,276**	**9,951**	**10,386**
LIABILITIES AND EQUITY					
Current liabilities:					
Accounts payable and accruals	17	1,086	1,000	20	16
Taxation payable		-	-	-	2
Short-term derivative liabilities	18	214	68	-	-
Short-term provisions	19	22	34	-	-
Debt due within one year	20	958	488	5,764	4,993
Total current liabilities		2,280	1,590	5,784	5,011
Non-current liabilities:					
Deferred tax liabilities	13	170	93	-	-
Long-term derivative liabilities	21	367	577	-	-
Long-term provisions	19	22	8	-	-
Long-term debt	22	1,830	2,404	2,846	2,442
Total non-current liabilities		2,389	3,082	2,846	2,442
Total liabilities		4,669	4,672	8,630	7,453
Equity:					
Share capital		1,297	2,270	1,297	2,270
Reserves		(15)	(84)	11	15
Retained earnings		1,447	1,412	13	648
Total equity attributable to equity holders of the Company		2,729	3,598	1,321	2,933
Minority interests		7	6	-	-
Total equity	23	2,736	3,604	1,321	2,933
Total liabilities and equity		**7,405**	**8,276**	**9,951**	**10,386**

On behalf of the board

WAYNE BOYD, Chairman PAUL REYNOLDS, Chief Executive Officer

Authorised for issue on 21 August 2008

See accompanying notes to the financial statements.

Cash flow statements

For the years ended 30 June 2008, 2007 and 2006

YEAR ENDED 30 JUNE		GROUP			PARENT	
(DOLLARS IN MILLIONS)	NOTES	2008 NZ$M	2007 NZ$M	2006 NZ$M	2008 NZ$M	2007 NZ$M
Cash flows from operating activities						
Cash was provided from/(applied to):						
Cash received from customers		5,583	5,726	5,740	-	-
Interest income		112	38	22	-	317
Dividend income		89	19	-	-	-
Dividends received from subsidiary companies		-	-	-	544	3,346
Payments to suppliers and employees		(3,739)	(3,706)	(3,484)	-	-
Income tax paid		(111)	(147)	(177)	-	-
Interest paid on debt		(249)	(279)	(294)	-	(396)
Net cash flows from operating activities	32	1,685	1,651	1,807	544	3,267
Cash flows from investing activities						
Cash was provided from/(applied to):						
Sale of property, plant and equipment		3	10	6	-	-
Sale/(purchase) of short-term investments, net		70	(7)	23	-	279
Sale of customer base		7	-	-	-	-
Sale of subsidiary companies, net of cash sold		-	2,163	-	-	-
Purchase of subsidiary companies, net of cash acquired		(4)	(347)	(8)	-	-
Purchase of long-term investments		(9)	(4)	(19)	(764)	(3,005)
Sale of long-term investments		-	-	293	1,074	-
Repayment of advance to associate		-	85	-	-	-
Purchase of property, plant and equipment		(945)	(861)	(737)	-	-
Capitalised interest paid		(12)	(11)	(11)	-	-
Net cash flows from investing activities		(890)	1,028	(453)	310	(2,726)
Cash flows from financing activities						
Cash was provided from/(applied to):						
Proceeds from long-term debt		-	376	397	-	-
Settlement of derivatives		(53)	62	-	-	-
Repayment of long-term debt and derivatives		(297)	(706)	(660)	-	-
Proceeds from/(repayment of) short-term debt, net		57	(87)	5	886	(49)
Capital contributed	23	-	-	11	-	1
Capital repurchased		(1,178)	-	(114)	(1,178)	-
Dividends paid		(565)	(497)	(1,073)	(562)	(493)
Net cash flows from financing activities		(2,036)	(852)	(1,434)	(854)	(541)
Net cash flow		(1,241)	1,827	(80)	-	-
Opening cash position		1,969	155	235	-	-
Foreign exchange movements		51	(13)	-	-	-
Closing cash position		**779**	**1,969**	**155**	**-**	**-**

See accompanying notes to the financial statements.

Notes to the financial statements

Note 1 Statement of accounting policies

Reporting entity and statutory base

Telecom Corporation of New Zealand Limited is a profit-orientated company registered in New Zealand under the Companies Act 1993, and is an issuer for the purposes of the Financial Reporting Act 1993.

The financial statements presented are those of Telecom Corporation of New Zealand Limited (the 'Company' or the 'Parent Company'), its subsidiaries and interests in associates (the 'Telecom group' or 'Telecom'). The Parent Company financial statements are presented in the consolidated financial statements in accordance with the requirement of the Financial Reporting Act 1993.

Nature of operations

Telecom is a major supplier of telecommunications and information technology services in New Zealand and Australia. Telecom provides a full range of telecommunications and information technology products and services including local, national, international and value-added telephone services, mobile services, data and internet services, IT consulting, implementation and procurement, equipment sales and installation services, and leased services.

Basis of preparation

These financial statements comply with International Financial Reporting Standards as issued by the International Accounting Standards Board (IFRS). They have been prepared in accordance with the Financial Reporting Act 1993 which requires compliance with accounting practice generally accepted in New Zealand. They comply with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS), and other applicable Financial Reporting Standards, as appropriate for profit-orientated entities.

The financial statements are expressed in New Zealand dollars which is the Company's functional currency. References in these financial statements to '$' and 'NZ$' are to New Zealand dollars, references to 'US$' and 'USD' are to US dollars, references to 'A$' and 'AUD' are to Australian dollars, references to 'JPY' are to Japanese Yen, references to 'EUR' are to Euros, references to 'CAD' are to Canadian dollars, references to 'DKK' are to Danish krone, and references to 'GBP' are to Pounds Sterling. All financial information has been rounded to the nearest million, unless otherwise stated.

Measurement basis

The measurement basis adopted in the preparation of these financial statements is historical cost, modified by the revaluation of certain investments and financial instruments as identified in specific accounting policies below and accompanying notes.

Specific accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements and have been applied consistently by all Telecom group companies. Certain comparative information has been reclassified to conform with the current year's presentation. In addition, the 2006 comparative income statement has been restated as if the operation that discontinued during the 2007 period had been discontinued at the start of 2006.

Basis of consolidation

Subsidiaries

Subsidiaries are entities controlled, directly or indirectly, by the Telecom group. All significant intercompany accounts and transactions are eliminated on consolidation.

Associates

Associates are entities in which the Telecom group has significant influence over, but not control over, the operating and financial policies.

Associate companies are reflected in the consolidated financial statements using the equity method, whereby Telecom's share of the post-acquisition net earnings of associates is included in consolidated earnings before income tax. Where the equity accounted carrying amount of an investment in an entity falls below zero, the equity method of accounting is suspended and the investment recorded at zero except where there is a legal or constructive obligation to fund those losses, in which case losses are recorded and a liability is recognised. If this occurs, the equity method of accounting is not resumed until such time as Telecom's share of losses and reserve decrements, not recognised during the financial years in which the equity method was suspended, are offset by the current share of earnings and reserves.

Goodwill

Goodwill represents the excess of purchase consideration over the fair value of net assets acquired at the time of acquisition of a business or shares in a subsidiary. Goodwill is allocated to cash-generating units and assessed annually for impairment and to the extent that it is no longer probable it will be recovered from future economic benefits of the related cash generating unit it is recognised immediately as an expense.

Acquisition or disposal during the year

Where an entity becomes or ceases to be a Telecom group entity during the year, the results of that entity are included in the net earnings of the Telecom group from the date that control or significant influence commenced or until the date that control or significant influence ceased.

Revenue recognition

Telecom recognises revenues as it provides services or delivers products to customers. Where products are sold in a bundle with a single price that price is allocated to each element of the bundle in proportion to the fair value of each element and recognised as appropriate for that element. Revenue is recognised to the extent that it is not contingent on the provision of a future service. Billings for telecommunications services (including fixed line, mobile, broadband and internet access billings) are made on a monthly basis. Unbilled revenues from the billing cycle date to the end of each month are recognised as revenue during the month the service is provided. Revenue is deferred in respect of the portion of fixed monthly charges that have been billed in advance.

Contract acquisition and origination costs are expenses as incurred.

Revenue from the sale of prepaid mobile minutes is initially deferred, with recognition occurring when the minutes are used by the customer. Revenue from installations and connections and related costs are recognised upon completion of the installation or connection. Revenue from equipment sales is recognised upon delivery of equipment to the customer. Revenue from IT solutions is recognised on a percentage of completion method and revenue is recognised based on costs incurred to date as a percentage of the estimated costs to fulfil the contract.

Accounts receivable

Accounts receivable are recorded initially at fair value and subsequently measured at amortised cost using the effective interest method, less any provision for impairment losses due to bad and doubtful accounts. The provision for doubtful debts is based on management's assessment of amounts considered uncollectible for specific customers or groups of customers based on age of debt, history of payments, account activity, economic factors and other relevant information. The amount of the provision is the difference between the assets unamortised cost and the present value of estimated future cash flows, discounted at an effective interest rate. The provision is recognised in the income statement.

Bad debts are written off against the provision for doubtful debts in the period in which it is determined that the debts are uncollectible. If those debts are subsequently collected then a gain is recognised in the income statement.

Inventories

Inventories are stated at the lower of cost and net realisable value after due consideration for excess and obsolete items. Cost is determined on a weighted average cost basis and amounts are removed from inventory on this basis. Cost of inventories includes the transfer from equity of any foreign exchange gains or losses on qualifying cash flow hedges related to inventories. Cash flows from the sale of inventories are included in amounts received from customers in the cash flow statement.

Financial instruments

Telecom's non-derivative financial instruments comprise investments in equity and debt securities, trade and other receivables, cash, loans and borrowings, trade and other payables.

Non-derivative financial instruments are recognised initially at fair value plus, for instruments not at fair value through profit and loss, any directly attributable transaction costs. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

A financial instrument is recognised if Telecom becomes a party to the contractual provisions of the instrument. Financial assets are de-recognised if Telecom's contractual rights to the cash flows from the financial assets expire or if Telecom transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset. Purchases and sales of financial assets are accounted for at trade date, ie, the date Telecom commits itself to purchase or sell the asset. Financial liabilities are de-recognised if Telecom's obligations specified in the contract expire or are discharged or cancelled.

Cash comprises cash balances and highly liquid call deposits. Bank overdrafts that are repayable on demand and form an integral part of Telecom's cash management are included as a component of cash for the purpose of the statement of cash flows.

Instruments at fair value through profit or loss

An instrument is classified at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Derivatives are also categorised as held for trading unless they are designated as hedges. Upon initial recognition, attributable transaction costs are recognised in profit or loss when incurred. Subsequent to initial recognition, financial instruments at fair value through profit or loss are measured at fair value, and changes therein are recognised in profit or loss.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These assets are carried at amortised cost using the effective interest method, less any impairment losses.

Held to maturity investments

Held-to-maturity investments are non-derivative financial assets which Telecom has the positive intent and ability to hold to maturity. Subsequent to initial recognition, held-to-maturity investments are measured at amortised cost using the effective interest method, less any impairment losses.

Available-for-sale financial assets

Telecom's investments in equity securities are classified as available-for-sale financial assets and are measured upon initial recognition at fair value. Subsequent to initial recognition, any changes in fair value, other than impairment losses and foreign exchange gains and losses on available-for-sale monetary items, are recognised directly in equity. When an investment is de-recognised, the cumulative gain or loss in equity is transferred to profit or loss. Where there is no reliable fair value the asset is carried at cost.

Where, in the opinion of the directors, there has been impairment in the value of investments this is recognised in the current period. In the case of equity securities classified as available-for-sale, losses arising from a significant or prolonged decline in the fair value are removed from equity and recognised in the income statement. Impairment losses recognised in the income statement on equity instruments are not reversed through the income statement.

Investments in subsidiaries in the Parent Company's separate accounts are held at cost.

Further specific information on Telecom's accounting policies on financial instruments is set out in Notes 12 and 26 of these financial statements.

Property, plant and equipment

Property, plant and equipment is valued as follows:

- The value of property, plant and equipment purchased from the Government was determined using deemed cost as at 1 April 1987
- Subsequent additions are recognised at cost. The cost of additions to plant and equipment and other assets constructed by Telecom consists of all appropriate costs of development, construction and installation, comprising material, labour, direct overhead and transport costs
- For each qualifying asset project, directly attributable interest costs incurred during the period required to complete and prepare the property, plant or equipment for its intended use are capitalised as part of the total cost

Depreciation
Depreciation is charged on a straight-line basis to write down the cost of property, plant and equipment to its estimated residual value over its estimated useful lives, which are as follows:

Telecommunications equipment and plant:	
Customer local access	3 - 50 years
Junctions and trunk transmission systems	10 - 50 years
Switching equipment	3 -15 years
Customer premises equipment	3 - 5 years
Other network equipment	4 - 25 years
Buildings	40 - 50 years
Motor vehicles	4 -10 years
Furniture and fittings	5 -10 years
Computer equipment	3 -5 years

Where the remaining useful lives or recoverable values have diminished due to technological change or market conditions, depreciation is accelerated.

Land and capital work in progress are not depreciated.

Where property, plant or equipment is disposed of, the profit or loss recognised in the income statement is calculated as the difference between the sale price and the carrying value of the asset.

Leased assets
Telecom is a lessor of equipment. Such leases are considered operating leases where substantially all the risks and rewards incidental to ownership remain with Telecom. Rental income is taken to revenue on a straight-line basis over the lease term.

Telecom is a lessee of certain plant, equipment, land and buildings under both operating and finance leases. Lease costs relating to operating leases are recognised straight-line. Finance leases, which effectively transfer to Telecom substantially all the risks and benefits of ownership of the leased assets, are capitalised at the lower of the leased assets fair value or the present value of the minimum lease payments at inception of the lease. The leased assets and corresponding liabilities are recognised and the leased assets are depreciated over their estimated useful lives.

Intangible assets
The cost of acquiring an intangible asset is amortised from the date the underlying asset is held ready for use on a straight-line basis over their estimated useful life which is as follows:

Software	2 - 8 years
Capacity purchases	10 -15 years
Spectrum licences	4 - 20 years
Other intangibles	1 - 20 years

Where estimated useful lives or recoverable values have diminished due to technological change or market conditions, amortisation is accelerated.

Telecom capitalises the direct costs associated with the development of network and business software for internal use where project success is regarded as probable. Capitalised costs include external direct costs of materials and services consumed, payroll and direct payroll-related costs for employees (including contractors) directly associated with the project and interest costs incurred while developing the software. Software developed for internal use is depreciated over its useful life.

Debt
Debt is recognised initially at fair value less attributable transactions costs. Subsequent to initial recognition, debt is stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest rate method.

Compensated absences
The liability for employees compensation for future absences, calculated on an actuarial basis, is accrued in respect of employee services already rendered and where the obligation relates to rights that may eventually vest.

Share-based compensation
Telecom operates three share-based compensation plans (see note 24 for details). The fair value of the employee services received in exchange for the grant of equity instruments is recognised as an expense. The total amount to be expensed over the vesting period is determined by reference to the fair value of the equity instruments granted, excluding the impact of any non-market vesting conditions. Non-market vesting conditions are included in assumptions about the number of equity instruments that are expected to become exercisable. At each balance sheet date, Telecom revises its estimates of the number of equity instruments that are expected to become exercisable. Telecom recognises the impact of the revision of original estimates, if any, in the income statement.

The proceeds received net of any directly attributable transaction costs are credited to contributed capital when equity instruments are exercised.

Research costs
Research costs are expensed as incurred.

Advertising costs
Advertising costs are expensed as incurred.

Government grants
Government grants are recognised in earnings on a systematic basis that matches them with the related costs that they are intended to compensate. To achieve this, grants that were made for Telecom to purchase assets are netted off against the cost of that asset.

Taxation
The taxation expense charged to earnings includes both current and deferred tax and is calculated after allowing for permanent differences.

Deferred taxation is recognised using the liability method, on temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Future tax benefits are recognised where realisation of the asset is probable.

Foreign currency transactions
Transactions denominated in a foreign currency are converted at the functional currency exchange rate at the date of the transaction. Foreign currency receivables and payables at balance date are translated at exchange rates existing at balance date. Exchange differences arising on the translation of accounts payable and receivable in foreign currencies are recognised in the income statement.

Exchange gains and losses and hedging costs arising on contracts entered into as hedges of firm commitments are deferred in equity as qualifying cash flow hedges until the date the underlying transactions impact on the determination of net earnings.

Where capital project commitments are hedged against foreign currency rate risk, the exchange difference on the hedging transaction up to the date of purchase and all other costs associated with the hedging transaction are deferred in equity and capitalised as part of the completed asset.

Other derivative transactions that provide effective economic hedges under the risk management policies of the group, but which do not

qualify for hedge accounting are recognised immediately in the income statement.

Translation of foreign group entities

The financial statements of each of the group's subsidiaries are prepared in the functional currency of that entity. Functional currency is determined for each entity based on factors such as the principal trading or financing currency. Assets and liabilities of these entities are translated at exchange rates existing at balance date. Revenue and expenses are translated at rates approximating the exchange rates ruling at the dates of the transactions. The exchange gain or loss arising on translation is recorded in the foreign currency translation reserve.

Derivative financial instruments

Telecom uses derivative financial instruments to reduce its exposure to fluctuations in foreign currency exchange rates, interest rates and electricity prices.

Each derivative which is designated as a hedge is classified as either:

- a hedge of the fair value of recognised assets or liabilities (a fair value hedge) or
- a hedge of a highly probable forecast transaction (a cash flow hedge) or
- a hedge of a net investment in foreign operations.

Gains and losses on fair value hedges are included in the income statement together with any changes in the fair value of the hedged asset or liability.

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges are initially recognised in equity. The gain or loss relating to the ineffective portion is recognised immediately in the income statement. Amounts accumulated in equity are recycled in the income statement in the periods when the hedged item will affect profit or loss. Alternatively, when the forecast transaction that is hedged results in a non-financial asset or liability, the gains and losses previously deferred in equity are transferred from equity and included in the initial measurement of the cost of the asset or liability. When a hedging instrument expires or is sold, or a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity until the underlying physical exposure occurs. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

The effective portion of any gain or loss on hedges of net investments in foreign operations is recognised in equity and the gain or loss relating to any ineffective portion is recognised immediately in the income statement. Gains and losses included in equity are included in the income statement when the foreign operation is disposed of.

For an instrument to qualify as a hedge, at the inception of the derivative transaction the relationship between hedging instruments and hedged items must be documented, as must Telecom's risk management objective and strategy for undertaking various hedge transactions. On an ongoing basis Telecom documents whether the hedges are highly effective in offsetting changes in fair values of cash flows or hedged items.

Derivative financial instruments that do not qualify or no longer qualify as hedges are stated at market values and any resultant gain or loss is recognised in the income statement.

The foreign exchange gains and losses on the principal value of cross currency interest rate swaps are reflected in the income statement using the spot rate which offsets the foreign exchange gains and losses recorded on the underlying hedged transaction.

Cash flows from derivatives are recognised in the cash flow statement in the same category as that of the hedged item.

Cash flow statement

For the purposes of the Cash Flow Statement, cash is considered to be cash on hand, in banks and cash equivalents, net of bank overdrafts and highly liquid investments that are readily convertible to known amounts of cash which are subject to an insignificant risk of changes in values.

Cash flows from certain items are disclosed net due to the short-term maturities and volume of transactions involved.

Earnings per share

The group presents basic and diluted earnings per share ('EPS') data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding for the effects of all dilutive potential ordinary shares, which comprise convertible notes and share options granted to employees.

Segment reporting

A segment is a distinguishable component of the Telecom group that is engaged in providing related products and services (business segment) which is subject to risks and rewards that are different from those of other segments. Telecom's primary format for segment reporting is based on business segments.

Impairment of assets

For the purpose of impairment testing, assets are grouped at the lowest levels for which there are separately identifiable cash flows where it is not possible to estimate the recoverable amount of an individual asset. If the recoverable amount of the cash-generating unit is less than the carrying amount of the unit, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets. Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate.

Discontinued operations

Discontinued operations represent a cash-generating unit that has been disposed of, and represented a separate major line of business. The net earnings from discontinued operations represent the post-tax profit of the discontinued operation together with the post-tax gain recognised on the disposal.

Critical accounting policies

The preparation of financial statements in conformity with NZ IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Actual results could differ from those estimates. The principal areas of judgement in preparing these financial statements are set out below.

Valuation of goodwill

The carrying value of goodwill is assessed at least annually to ensure that it is not impaired. Performing this assessment generally requires management to estimate future cash flows to be generated by the related investment, which entails making judgements including the expected rate of growth of revenues, margins expected to be achieved, the level of future capital expenditure required to support these outcomes and the appropriate discount rate to apply when valuing future cash flows.

At 30 June 2008 Telecom had recognised NZ$170 million of goodwill on its balance sheet (30 June 2007: NZ$159 million). The composition of this balance, by cash-generating unit, is set out in note 15 of these financial statements. No impairment arose as a result of the review of goodwill for the years ended 30 June 2008 and 30 June 2007, however the carrying value of NZ$834 million of goodwill relating to past Australian acquisitions was fully written off in the year ended 30 June 2006.

Any future adverse impacts arising in assessing the carrying value of Telecom's goodwill could lead to material future goodwill impairment that could affect future earnings.

Valuation of long-term investments

Management performs an assessment of the carrying value of long-term investments at each reporting period. In assessing whether there has been an impairment, consideration is given to the financial performance of the investee and other factors that impact management's expectation of recovering the value of the investment. This assessment also requires management to make judgements about the expected future performance and cash flows of the investee, and an appropriate discount rate.

At 30 June 2008 Telecom had recognised NZ$527 million of long-term investments on its balance sheet (30 June 2007: NZ$494 million) as described in notes 12 and 26 of these financial statements. No impairment arose relating to long-term investments in the three-year period ending 30 June 2008, however any future adverse impacts arising in assessing the carrying value of Telecom's long-term investments could lead to material future impairments that would affect future earnings. Telecom carries its investment in Hutchison (see note 12) at cost as there is no reliable estimate of fair value for this estimate, including the quoted share price.

Accounting for property, plant and equipment and finite-lived intangible assets

In accounting for the creation of items of property, plant and equipment and finite-lived intangible assets, judgements must be made about whether costs incurred relate to bringing an asset to working condition for its intended use and therefore are appropriate for capitalisation as part of the cost of the asset or whether they should be expensed as incurred. In capitalising costs for internally constructed assets, judgements must be made about the likelihood of project success. Such judgements can be difficult where the project involves the application of unproven technology.

The determination of the appropriate useful life for a particular asset requires management to make judgements about, among other factors, the expected period of service potential of the asset, the likelihood of the asset becoming obsolete as a result of technological advances, and the likelihood of Telecom ceasing to use the asset in its business operations.

Assessing whether an asset is impaired may involve estimating the future cash flows that the asset is expected to generate. This will in turn involve a number of assumptions, including rates of expected revenue growth or decline, expected future margins and the selection of an appropriate discount rate for valuing future cash flows.

At 30 June 2008 Telecom's balance sheet had a carrying value of NZ$4,804 million in relation to property, plant and equipment and finite-lived intangible assets (30 June 2007: NZ$4,449 million). No impairment arose as a result of the review of the carrying value of these assets for the years ended 30 June 2008 and 30 June 2007. NZ$467 million of assets relating to Australian operations was impaired in the year ended 30 June 2006.

Any future adverse impacts arising in assessing the carrying value of Telecom's property, plant and equipment and finite-lived intangible assets could lead to material future impairments that could affect future earnings.

Provision for doubtful debts

Telecom maintains a provision for estimated losses expected to arise from customers being unable to make required payments. This provision takes into account known commercial factors impacting specific customer accounts, as well as the overall profile of Telecom's debtors' portfolio. In assessing the provision, factors such as past collection history, the age of receivable balances, the level of activity in customer accounts, as well as general macro-economic trends, are taken into account.

At 30 June 2008 the provision for doubtful debts was NZ$32 million compared to NZ$44 million at 30 June 2007. The 2008 provision represents 6.0% of gross trade receivables (30 June 2007: 7.5%) and during the year to 30 June 2008 NZ$41 million was written off against the provision account (30 June 2007: NZ$28 million). Any future increase or decrease in the amount of provisioning required for doubtful debts will increase or decrease future pre-tax earnings by the same amount.

Accounting for interconnection revenues and expenses

In the course of its normal business operations Telecom interconnects its networks with other telecommunications operators. In some instances management may be required to estimate levels of traffic flows between networks in order to determine amounts receivable or payable for interconnection.

The terms of interconnection, including pricing, are subject to regulation in some instances. Pricing may be subject to retrospective adjustment, in which case estimates of the likely effect of these adjustments are required in order to determine revenues and expenses. Likewise, where interconnection rates are in dispute with another carrier, estimates of the likely outcome of disputes are required to determine financial results. Telecom bases these estimates on management's interpretation of material facts, as well as independent advice.

Any future decrease in the amounts of interconnection revenues and expenses will have a corresponding impact on Telecom's pre-tax earnings when recognised.

Accounting for income taxes

Preparation of financial statements requires management to make estimates as to, amongst other things, the amount of tax that will ultimately be payable, the availability of losses to be carried forward and the amount of foreign tax credits that it will receive. Actual results may differ from these estimates as a result of reassessment by management or taxation authorities.

At 30 June 2008 Telecom had a current tax receivable of NZ$93 million (30 June 2007: a receivable of NZ$8 million). At 30 June 2008 Telecom had recognised NZ$52 million of deferred tax assets in relation to tax loss carry forwards (30 June 2007: NZ$66 million). As described in note 13 to the financial statements, the utilisation of deferred tax assets is dependent on future taxable profits and Telecom has continued to recognise these based on its forecasts of future taxable earnings. If Telecom's forecast of future taxable profits were to decline such that an impairment of these tax losses arose, the amount impaired will have the effect of increasing the tax expense in that period.

At 30 June 2008 Telecom had NZ$298 million of tax losses and other temporary differences not currently recognised (30 June 2007: NZ$461 million). An increase in Telecom's expected future taxable profits relating to these unrecognised losses could result in additional deferred tax assets being recognised.

Note 2 Operating revenues and other gains

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	GROUP 2007 NZ$M	GROUP 2006 NZ$M	PARENT 2008 NZ$M	PARENT 2007 NZ$M
Sale of goods	305	312	283	-	-
Rendering of services	5,272	5,231	5,212	-	-
Dividends	89	19	-	544	3,347
Other gains	7	20	60	-	-
Total operating revenue and other gains	**5,673**	**5,582**	**5,555**	**544**	**3,347**

Rendering of services has been restated in 2007 to exclude dividends which are now presented separately.

Note 3 Calling and other operating revenues

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	GROUP 2007 NZ$M	GROUP 2006 NZ$M	PARENT 2008 NZ$M	PARENT 2007 NZ$M
Calling					
National	753	816	897	-	-
International	432	472	442	-	-
Other	48	48	46	-	-
	1,233	**1,336**	**1,385**	**-**	**-**
Other operating revenues					
Resale	360	399	363	-	-
Equipment	45	52	55	-	-
Miscellaneous other	175	164	145	-	-
Dividends	89	19	-	544	3,347
	669	**634**	**563**	**544**	**3,347**

Note 4 Operating expenses

Labour

Included in labour costs are pension contributions of NZ$1 million to the New Zealand Government Superannuation Fund (30 June 2007: NZ$1 million; 30 June 2006: NZ$1 million) and NZ$15 million on behalf of Australian employees as required by the Superannuation Guarantee (Administration) Act 1992 (30 June 2007: NZ$14 million; 30 June 2006: NZ$14 million). Telecom also commenced making employer contributions under the KiwiSaver and Company Tax Rate Amendments Act 2007 in 2008. Telecom has no other obligations to provide pension benefits in respect of employees.

Other operating expenses

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	GROUP 2007 NZ$M	GROUP 2006 NZ$M
Other operating expenses include:			
Direct costs	352	326	279
Mobile acquisition, updates and dealer commissions	280	312	317
Procurement and IT services expenses	264	222	180
Computer costs	197	194	162
Advertising costs	90	129	143
Broadband and internet	67	80	73
Accommodation – other costs	66	52	51
Accommodation – lease and rental costs	61	59	54
Outsourcing	52	26	23
Provision for doubtful debts	29	33	34
Equipment – lease and rental costs	11	11	12
Research costs	9	10	9
Movement in provision for inventory obsolescence	6	-	(4)
Directors' fees	2	2	2
Foreign exchange (gains)/losses	(1)	2	(8)
Gain on disposal of property, plant and equipment	(3)	(1)	(1)
Other	171	146	171
Total other operating expenses	**1,653**	**1,603**	**1,497**

Key management personnel costs

	GROUP		
YEAR ENDED 30 JUNE	2008	2007	2006
(DOLLARS IN THOUSANDS)	NZ$000S	NZ$000S	NZ$000S
Salary and other short-term benefits	12,181	12,340	8,435
Redundancy and termination payments	1,250	1,538	519
Share-based compensation	3,376	2,300	2,244
	16,807	**16,178**	**11,198**

The table above includes remuneration of the Chief Executive Officer and the members of the executive team.

Auditors' remuneration

	GROUP		
YEAR ENDED 30 JUNE	2008	2007	2006
(DOLLARS IN THOUSANDS)	NZ$000S	NZ$000S	NZ$000S
Fees billed by principal accountants:			
Audit fees	3,815	4,463	2,615
Audit related fees	461	533	1,023
Total fees billed by principal accountants	**4,276**	**4,996**	**3,638**

Audit related fees primarily relate to the audit of regulatory disclosures such as the Telecom List of Charges and the Telecom Service Obligation ('TSO') as required by telecommunications legislation. For the year ended 30 June 2006, audit related fees also included preparatory work for compliance with section 404 of the US Sarbanes-Oxley Act of 2002. All fees billed to the principal accountants were pre-approved by the Audit and Risk Management Committee. There were no tax fees or other fees for the periods specified.

Donations

The donation expense for the year was NZ$1,010,000 (30 June 2007: NZ$64,000; 30 June 2006: NZ$127,000).

Note 5 Other gains, expenses and impairment

	GROUP			PARENT	
YEAR ENDED 30 JUNE	2008	2007	2006	2008	2007
(DOLLARS IN MILLIONS)	NZ$M	NZ$M	NZ$M	NZ$M	NZ$M
Other Gains					
Sale of Australian mobile customer base	7	-	-	-	-
Gain on sale of TSCL	-	20	-	-	-
Gain on acquisition of SCCL	-	-	60	-	-
	7	**20**	**60**	**-**	**-**
Impairment					
Impairment of Australian Operations	-	-	1,301	-	-
	-	**-**	**1,301**	**-**	**-**
Other Expenses					
Restructuring costs	-	36	-	-	-
Provision for billing issues	-	16	-	-	-
Intercarrier and regulatory costs	-	-	22	-	-
Provision for contractual settlements	-	-	12	-	-
Intercompany balances	-	-	-	423	638
	-	**52**	**34**	**423**	**638**

Other gains

Gain on sale of Australian mobile customer base

In July 2007 Telecom sold its Australian mobile customer base resulting in a gain of NZ$7 million.

Gain on sale of Telecom Samoa Cellular Limited ('TSCL')

In the year ended 30 June 2007 Telecom announced the sale of its 90% share in TSCL to Digicel Samoa Limited resulting in a gain on sale of NZ$20 million.

Gain on acquisition of Southern Cross Cables (NZ) Limited ('SCCL')

In the year ended 30 June 2006 Telecom acquired a 100% shareholding in SCCL, a wholly-owned subsidiary of Southern Cross Cables in which Telecom holds a 50% shareholding. SCCL's sole asset at the time of acquisition was a tax operating loss carry forward. The value of the tax loss carry forward was NZ$70 million and Telecom's acquisition cost was NZ$10 million. The value in excess of Telecom's acquisition cost was reflected as a gain.

Impairment

Impairment of Australian Operations

Telecom reviewed the carrying value of the assets relating to its Australian Operations (which is a reportable segment). Prior to the write-down these assets had a total carrying value of A$1,464 million, including A$778 million of goodwill resulting from the purchase of AAPT. The recoverable amount for Telecom's Australian Operations was assessed on a value-in-use basis.

In previous periods the recoverable amount determined exceeded the carrying value. However, through assessments performed during the year ended 30 June 2006 it was determined that the recoverable amount was significantly lower than the carrying value and hence impairments were deemed to have occurred.

The decline in the recoverable amount was a consequence of a number of negative trends that adversely affected the short and long-term earnings outlook for Australian Operations, in particular:

- A significant tightening of wholesale prices and terms with Telstra Corporation Limited (the principal supplier to Telecom's Australian operations)
- Continued downward pressure on retail prices
- The deferral of major project expenditure by key corporate customers.

These fundamental changes in the industry, and revised expectations for implementation of new strategies within the Australian Operations, led to the recognition of impairment charges of NZ$1,301 million (A$1,163 million) in the year ended 30 June 2006. As a result of these impairments, all remaining goodwill resulting from Telecom's acquisition of AAPT was written off.

Other expenses

Restructuring costs

Restructuring costs totalling NZ$36 million were recognised in the year ended 30 June 2007 as a result of restructuring activities, including a company-wide organisational redesign programme, the costs of rationalising Australian call centre operations and the integration of PowerTel.

The costs associated with the organisational redesign programme are principally severance costs. The costs associated with the rationalisation of Australian call centre operations consisted of both personnel-related costs and the cost of surplus lease commitments.

Provision for billing issues

A provision of NZ$16 million for the cost of rectifying several billing application configuration issues largely relating to prior periods was recognised in the year ended 30 June 2007. The provision covers the cost of investigating and resolving these issues.

Intercarrier and regulatory costs

In the year ended 30 June 2006 Telecom and TelstraClear Limited reached an agreement that settled a number of longstanding commercial issues between the two companies, principally involving backdating of pricing of interconnection and wholesale arrangements. To settle these historical issues, Telecom agreed to make a one-off payment of NZ$18 million to TelstraClear.

In the year ended 30 June 2006 an adjustment was made to reflect a determination by the Commerce Commission that resulted in a one-off adjustment to the accrued TSO receivable of NZ$4 million.

Contractual settlements

In the year ended 30 June 2006, Telecom recognised NZ$7 million for the estimated liability relating to historic issues under the Fair Trading Act and the Door to Door Sales Act 1967. Telecom also recognised NZ$5 million for the cost of terminating an agreement with Hutchison Whampoa Limited to receive 3G mobile services for Telecom's New Zealand business.

Parent company

Intercompany balances

NZ$404 million (30 June 2007: NZ$216 million) represented the movement in the value of a guarantee reflecting intercompany obligations of subsidiary companies assumed by the Parent. In addition a write-down of investments in subsidiaries of NZ$19 million was recognised (30 June 2007: NZ$422 million).

Note 6 Finance income and expense

	GROUP			PARENT	
YEAR ENDED 30 JUNE	2008	2007	2006	2008	2007
(DOLLARS IN MILLIONS)	NZ$M	NZ$M	NZ$M	NZ$M	NZ$M
Finance income:					
Interest income from deposits	98	59	28	-	-
Other interest income	21	-	-	-	-
Interest income from subsidary companies	-	-	-	311	317
Finance income	**119**	**59**	**28**	**311**	**317**
Finance expense:					
Finance expense on long-term debt:					
- Euro Medium Term Notes	203	225	224	-	-
- Capital Notes	10	16	28	-	-
- Telebonds	36	42	31	-	-
Revaluation of interest rate derivative	(4)	2	-	-	-
Other interest and finance expenses	38	15	10	-	-
Interest expense from subsidiary companies	-	-	-	432	396
	283	300	293	432	396
Less interest capitalised	(12)	(11)	(11)	-	-
Finance expense	**271**	**289**	**282**	**432**	**396**

Interest is capitalised on property, plant and equipment and intangible assets under development at an annualised rate of 8% (30 June 2007: 8%; 30 June 2006: 8%).

Note 7 Income tax

The income tax (expense)/credit is determined as follows:

	GROUP			PARENT	
YEAR ENDED 30 JUNE	2008	2007	2006	2008	2007
(DOLLARS IN MILLIONS)	NZ$M	NZ$M	NZ$M	NZ$M	NZ$M
Income statement					
Current income tax					
Current year income tax (charge)/credit	(191)	(219)	(308)	40	26
Adjustments in respect of prior periods	13	(11)	(1)	-	-
Deferred income tax					
Depreciation	(58)	(18)	(54)	-	-
Provisions, accruals, tax losses and other	(24)	10	5	-	-
Adjustments in respect of prior periods	(2)	17	7	-	-
Reduction in tax rate	-	16	-	-	-
Income tax (charge)/credit reported in income statement	**(262)**	**(205)**	**(351)**	**40**	**26**
Statement of changes in equity					
Current income tax					
Current year income tax (charge)/credit	70	(49)	100	-	-
Deferred income tax					
Fair value of derivative financial instruments	(23)	3	(3)	-	-
Revaluation of listed investments	3	(4)	-	-	-
Reduction in tax rate	-	(1)	-	-	-
Income tax (charge)/credit reported in equity	**50**	**(51)**	**97**	**-**	**-**

Reconciliation of income tax expense

	Group			Parent	
Year ended 30 June	2008	2007	2006	2008	2007
(Dollars in millions)	NZ$M	NZ$M	NZ$M	NZ$M	NZ$M
Net earnings/(loss) for the year	713	3,027	(431)	40	2,656
Total income tax expense/(credit)	262	246	394	(40)	(26)
Net earnings/(loss) before income tax	975	3,273	(37)	-	2,630
Tax at current rate of 33%	(322)	(1,080)	12	-	(868)
Adjustment to taxation:					
Non-deductible expenses	(8)	-	(420)	(140)	(210)
Non-taxable gain	-	695	20	-	-
Foreign sourced income with lower effective tax rate	81	24	8	-	-
Non-taxable intercompany dividends	-	-	-	180	1,104
Reduction in tax rate	-	16	-	-	-
Change in unrecognised temporary differences	(4)	99	-	-	-
Prior period adjustment	11	6	-	-	-
Current year loss not recognised as an asset	(4)	-	(18)	-	-
Write-off of previously recognised temporary differences	(20)	-	-	-	-
Other	4	(6)	4	-	-
Total income tax (expense)/credit	**(262)**	**(246)**	**(394)**	**40**	**26**
Income tax expense for continuing operations	(262)	(205)	(351)		
Income tax expense for discontinued operations	-	(41)	(43)		

On 21 May 2007, the Taxation KiwiSaver and Company Tax Rate Amendments Act 2007 was given royal assent meaning that for the 2008/09 income tax year the New Zealand company tax rate will change from 33% to 30%. The effect of the reduction in the tax rate on the measurement of deferred tax assets and liabilities has been shown in the table above.

The change in unrecognised temporary differences in 2007 consisted of NZ$99 million of previously unrecognised temporary differences that were recognised during the year after it became probable that these temporary differences would be offset against taxable income.

Note 8 Short-term investments

	Group	
30 June	2008	2007
(Dollars in millions)	NZ$M	NZ$M
Short-term deposits	-	70
	-	**70**

Note 9 Short-term derivative assets

	Group	
30 June	2008	2007
(Dollars in millions)	NZ$M	NZ$M
Foreign currency forward contracts	9	7
Currency options	2	-
Electricity swap	3	-
Interest rate swaps	1	1
	15	**8**

Note 10 Receivables and prepayments

30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	GROUP 2007 NZ$M	PARENT 2008 NZ$M	PARENT 2007 NZ$M
Trade receivables	530	588	-	-
Less allowance for doubtful accounts receivable	(32)	(44)	-	-
	498	544	-	-
Unbilled rentals and tolls	301	278	-	-
Prepaid expenses and other receivables	113	131	-	-
Due from subsidiaries	-	-	689	795
	912	**953**	**689**	**795**

Bad debts of NZ$41 million (30 June 2007: NZ$28 million) were written off against the allowance for doubtful accounts during the year.

Note 11 Inventories

30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	GROUP 2007 NZ$M
Maintenance materials and consumables	7	5
Goods held for resale	38	59
Revenue work in progress	12	7
	57	**71**
Allowance for inventory obsolescence:		
Balance at beginning of period	-	-
Charged to costs and expenses	(6)	-
Balance at end of period	(6)	-

Note 12 Long-term investments

30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	GROUP 2007 NZ$M	PARENT 2008 NZ$M	PARENT 2007 NZ$M
Shares in Hutchison	449	416	-	-
Shares in other listed companies	51	51	-	-
Shares in unlisted companies	23	23	-	-
Government stock	1	1	-	-
Investment in associates	3	3	-	-
Subsidiary companies (see Note 30)				
Shares	-	-	6,256	6,585
Term advances	-	-	3,006	3,006
	527	**494**	**9,262**	**9,591**

Shares in Hutchison

The shares in Hutchison represent Telecom's investment in Hutchison Telecommunication's Australian operations ('Hutchison'). At 30 June 2008 the investment related to a 10% interest in Hutchison Telecommunications Australia Limited (2007: 19.9% interest in Hutchison 3G Australia Limited). During the year ended 30 June 2008 Telecom exchanged its interest in Hutchison 3G Australia Limited for a 10% interest in Hutchison Telecommunications Australia Limited and an option to acquire a further 9.9%. The option has a strike price of A$300 million and expires in December 2008. Telecom holds its investments in Hutchison at cost, as described in note 26. The increase in the investment during the year 30 June 2008 related to foreign exchange rate movements.

Shares in other listed companies

Shares in other listed companies represent Telecom's investment in Macquarie Telecom Group Limited and iiNet Limited. These investments are carried at fair value that is determined by reference to the bid price as quoted on the Australian Stock Exchange at the financial year end. The amount in the revaluation reserve relates solely to these investments.

Shares in unlisted companies

Shares in other unlisted companies relate to Telecom's investment in TMT Ventures, a corporate venture capital programme. This equity investment is held at cost as the fair value cannot be measured reliably.

Associate companies

Associate companies of the Telecom group are listed in Note 30.

30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	2007 NZ$M
Cost of investment in associates	41	38
Opening balance of share of associates' equity	(35)	(31)
Share of associates' losses	(3)	(3)
Foreign exchange movement	-	(1)
Equity accounted value of investment	**3**	**3**

Extract from associates financial statements

30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$	2007 NZ$
Total assets	1,435	1,244
Total liabilities	2,214	1,783
Total revenues	200	200
Net (loss)/earnings	**(61)**	**(6)**

Telecom ceased to recognise a share of net losses on its associates where its share of losses and dividends received have exceeded the initial investment. As at 30 June 2008 the cumulative deficit of associates was NZ$417 million (30 June 2007: NZ$292 million). As at 30 June 2008 Telecom has not recognised cumulative losses of NZ$159 million (30 June 2007: NZ$127 million) and has recognised cumulative dividend income of NZ$352 million (30 June 2007: NZ$263 million) from these associates. Telecom has no obligation to fund these losses. Telecom's share of profits not recognised for the year was nil (2007: nil)

Note 13 Deferred tax

GROUP 30 JUNE 2008 (DOLLARS IN MILLIONS)	TAX DEPRECIATION NZ$M	PROVISIONS AND ACCRUALS NZ$M	TAX LOSSES NZ$M	OTHER NZ$M	TOTAL NZ$M
Deferred tax					
Balance at beginning of the year	(196)	46	66	18	(66)
Amounts recognised in earnings					
Relating to the current period	(58)	(14)	(14)	4	(82)
Adjustments in respect of prior periods	-	(2)	-	-	(2)
Amounts recognised in equity					
Relating to the current period	-	-	-	(20)	(20)
Deferred tax liabilities	**(254)**	**30**	**52**	**2**	**(170)**

GROUP 30 JUNE 2007 (DOLLARS IN MILLIONS)	TAX DEPRECIATION NZ$M	PROVISIONS AND ACCRUALS NZ$M	TAX LOSSES NZ$M	OTHER NZ$M	TOTAL NZ$M
Deferred tax					
Balance at beginning of the year	(218)	29	70	33	(86)
Amounts recognised in earnings					
Relating to the current period	(18)	19	(3)	(6)	(8)
Adjustments in respect of prior periods	19	(2)	-	-	17
Reduction in tax rate	21	-	(5)	-	16
Amounts recognised in equity					
Relating to the current period	-	-	-	(1)	(1)
Foreign exchange movement	-	-	-	(3)	(3)
Reduction in tax rate	-	-	-	(1)	(1)
Other					
Amounts relating to acquisition of subsidiary	-	-	4	(4)	-
	(196)	**46**	**66**	**18**	**(66)**
Deferred tax assets	-	-	4	23	27
Deferred tax liabilities	(196)	46	62	(5)	(93)
	(196)	**46**	**66**	**18**	**(66)**

As at 30 June 2008, the utilisation of the deferred tax asset relating to tax losses is dependent on future taxable profits of approximately NZ$174 million and is subject to compliance with the relevant taxation authority requirements.

Telecom has continued to recognise these deferred tax assets as it is probable that there will be available taxable profits to offset these losses based on current forecasts and recent taxable profits.

The Telecom group has not recognised in its deferred taxation balance the tax effect of accumulated losses and temporary differences in overseas subsidiaries amounting to NZ$298 million at 30 June 2008 (30 June 2007: NZ$461 million), based on the relevant corporation tax rate of the overseas subsidiary's country of residence. These losses and temporary differences may be available to be carried forward to offset against future taxable income, however utilisation is contingent on the relevant subsidiaries producing taxable profits over a significant period of time and is subject to compliance with the relevant taxation authority requirements. As at 30 June 2008 NZ$5 million of these accumulated losses expire through to 2015 if not utilised.

As at 30 June 2008, the aggregate amount of temporary differences associated with undistributed earnings of subsidiaries for which deferred tax liabilities have not been recognised is NZ$45 million (30 June 2007: NZ$32 million). No liability has been recognised in respect of these differences because Telecom is in a position to control the timing of the reversal of the temporary differences and it is probable that such differences will not reverse in the foreseeable future.

Note 14 Long-term derivative assets

	GROUP	
30 JUNE	2008	2007
(DOLLARS IN MILLIONS)	NZ$M	NZ$M
Interest rate swap contracts	48	68
	48	**68**

Note 15 Intangible assets

GROUP 30 JUNE 2008 (DOLLARS IN MILLIONS)	SOFTWARE NZ$M	CAPACITY PURCHASES NZ$M	SPECTRUM LICENCES NZ$M	OTHER INTANGIBLES NZ$M	GOODWILL NZ$M	TOTAL NZ$M
Cost						
Balance as at 1 July 2007	1,377	486	57	30	993	2,943
External acquisitions	203	16	-	6	4	229
Disposals	(137)	(2)	(3)	(1)	-	(143)
Currency movements	45	-	-	-	113	158
Balance as at 30 June 2008	1,488	500	54	35	1,110	3,187
Accumulated amortisation and impairment losses						
Balance as at 1 July 2007	(976)	(168)	(21)	(17)	(834)	(2,016)
Amortisation	(143)	(39)	(3)	(2)	-	(187)
Disposals	137	2	2	1	-	142
Currency movements	(30)	-	-	-	(106)	(136)
Balance as at 30 June 2008	(1,012)	(205)	(22)	(18)	(940)	(2,197)
Net book value at 30 June 2008	**476**	**295**	**32**	**17**	**170**	**990**

GROUP 30 JUNE 2007 (DOLLARS IN MILLIONS)	SOFTWARE NZ$M	CAPACITY PURCHASES NZ$M	SPECTRUM LICENCES NZ$M	OTHER INTANGIBLES NZ$M	GOODWILL NZ$M	TOTAL NZ$M
Cost						
Balance as at 1 July 2006	1,211	462	57	32	939	2,701
External acquisitions	232	30	-	2	63	327
Disposals	-	-	-	(4)	-	(4)
Disposal of subsidiaries	(42)	-	-	-	(9)	(51)
Currency movements	(24)	(6)	-	-	-	(30)
Balance as at 30 June 2007	1,377	486	57	30	993	2,943
Accumulated amortisation and impairment losses						
Balance as at 1 July 2006	(871)	(129)	(19)	(19)	(834)	(1,872)
Amortisation	(110)	(41)	(2)	(3)	-	(156)
Reclassification	(39)	-	-	-	-	(39)
Disposals	-	-	-	4	-	4
Disposal of subsidiaries	29	-	-	-	-	29
Currency movements	15	2	-	1	-	18
Balance as at 30 June 2007	(976)	(168)	(21)	(17)	(834)	(2,016)
Net book value at 30 June 2007	**401**	**318**	**36**	**13**	**159**	**927**

Goodwill

Telecom's operating segments are determined to be cash-generating units, being the lowest level of asset for which there are separately identifiable cash flows. Goodwill by operating segment is presented below:

30 June (Dollars in millions)	Group 2008 NZ$M	Group 2007 NZ$M
Australian Operations	70	63
NZ Business	75	71
NZ Consumer	24	24
Corporate and other	1	1
	170	**159**

Impairment testing

The recoverable amount of each segment was calculated on the basis of value-in-use using a discounted cash flow model. Future cash flows were projected out five years, based on board-approved business plans for the year ended 30 June 2009, with key assumptions being segment earnings excluding depreciation and amortisation expense and capital expenditure for the segment. A terminal growth rate of between nil and 3% was applied. A pre-tax discount rate of between 13.4% and 14.7% was utilised. No impairment arose as a result of the review of goodwill for the year ended 30 June 2008. In relation to Australian Operations an increase of 1% in the discount rate or a decrease of 3% in the forecast earnings would result in an impairment. Telecom impaired goodwill in the year ended 30 June 2006 (see note 5).

Note 16 Property, plant & equipment

Group (Dollars in millions)	Telecommunications equipment and plant NZ$M	Freehold land NZ$M	Buildings NZ$M	Other assets NZ$M	Work in progress NZ$M	Total NZ$M
Cost						
Balance as at 1 July 2007	9,542	94	632	549	362	11,179
Acquisitions	281	-	37	83	403	804
Reclassification and transfers	278	-	(4)	(45)	(229)	-
Disposals	(468)	-	(84)	(165)	-	(717)
Currency movements	235	-	8	15	-	258
Balance as at 30 June 2008	9,868	94	589	437	536	11,524
Accumulated depreciation and impairment losses						
Balance as at 1 July 2007	(6,662)	-	(369)	(467)	-	(7,498)
Depreciation charge	(496)	-	(26)	(52)	-	(574)
Reclassification	(79)	-	3	76	-	-
Disposals	468	-	84	163	-	715
Currency movements	(162)	-	(9)	(12)	-	(183)
Balance as at 30 June 2008	(6,931)	-	(317)	(292)	-	(7,540)
Net book value at 30 June 2008	**2,937**	**94**	**272**	**145**	**536**	**3,984**

Group (Dollars in millions)	Telecommunications equipment and plant NZ$M	Freehold land NZ$M	Buildings NZ$M	Other assets NZ$M	Work in progress NZ$M	Total NZ$M
Cost						
Balance as at 1 July 2006	9,774	94	623	485	121	11,097
Acquisitions	427	-	21	58	83	589
Acquisition of subsidiary	459	-	4	51	-	514
Reclassification and transfers	(45)	-	-	(16)	178	117
Disposals	(970)	-	(3)	(8)	-	(981)
Disposal of subsidiaries	(12)	-	(9)	(12)	(13)	(46)
Currency movements	(91)	-	(4)	(9)	(7)	(111)
Balance as at 30 June 2007	9,542	94	632	549	362	11,179
Accumulated depreciation and impairment losses						
Balance as at 1 July 2006	(7,031)	-	(356)	(409)	-	(7,796)
Depreciation charge	(452)	-	(20)	(30)	-	(502)
Acquisition of subsidiary	(126)	-	(3)	(77)	-	(206)
Reclassification	(106)	-	-	28	-	(78)
Disposals	963	-	2	5	-	970
Disposal of subsidiaries	5	-	5	8	-	18
Currency movements	85	-	3	8	-	96
Balance as at 30 June 2007	(6,662)	-	(369)	(467)	-	(7,498)
Net book value at 30 June 2007	**2,880**	**94**	**263**	**82**	**362**	**3,681**

Values ascribed to land and buildings

Telecom's properties consist primarily of special-purpose network buildings, which form an integral part of the telecommunications network.

Operating leases

Included in buildings at 30 June 2008 are buildings on leasehold land with a cost of NZ$12 million (30 June 2007: NZ$12 million) together with accumulated depreciation of NZ$5 million (30 June 2007: NZ$4 million).

Finance leases

Included in telecommunications equipment at 30 June 2008 are assets capitalised under finance leases with a cost of $656 million (30 June 2007: NZ$680 million) together with accumulated depreciation of NZ$605 million (30 June 2007: NZ$593 million).

Telecom has prepaid all obligations under these finance leases and as a result has no outstanding commitments under finance leases.

Land claims

Under the Treaty of Waitangi Act 1975, all interests in land included in the assets purchased from the New Zealand Government may be subject to claims to the Waitangi Tribunal, which has the power to recommend, in appropriate circumstances, with binding effect, that the land be resumed by the Government in order that it be returned to Māori claimants. In the event that the Government resumes land, compensation will be paid to Telecom under the provisions of the Public Works Act 1981. If this is insufficient to cover the loss, certain additional compensation is payable under the provisions of the Sale and Purchase Agreement between the Company and the Government.

Under the State Owned Enterprises Act 1986, the Governor General of New Zealand, if satisfied that any land or interest in land held by Telecom is wāhi tapu (being land of special spiritual, cultural or historical tribal significance), may declare by Order in Council that the land be resumed by the Government, with compensation payable to Telecom under the provisions of the Public Works Act 1981. Telecom would expect to negotiate with the new Māori owners for continued occupancy rights of any sites resumed by the Government.

Note 17 Accounts payable and accruals

	GROUP		PARENT	
30 JUNE	2008	2007	2008	2007
(DOLLARS IN MILLIONS)	NZ$M	NZ$M	NZ$M	NZ$M
Trade accounts payable	780	708	-	-
Accrued personnel costs	130	117	-	-
Revenue billed in advance	98	109	-	-
Accrued interest	31	37	-	-
Other accrued expenses	47	29	20	16
	1,086	**1,000**	**20**	**16**

Note 18 Short-term derivative liabilities

	GROUP	
30 JUNE	2008	2007
(DOLLARS IN MILLIONS)	NZ$M	NZ$M
Cross currency interest rate swaps	187	43
Forward currency forward contracts	27	25
	214	**68**

Note 19 Provisions

GROUP	COMMERCIAL	RESTRUCTURING	OTHER	TOTAL
(DOLLARS IN MILLIONS)	NZ$M	NZ$M	NZ$M	NZ$M
Balance at 1 July 2007	16	18	8	42
Provisions made during the year	2	7	14	23
Provisions utilised during the year	(9)	(13)	-	(22)
Foreign exchange movements	-	-	1	1
Balance as at 30 June 2008	**9**	**12**	**23**	**44**
Current	9	12	1	22
Non-current	-	-	22	22
	9	**12**	**23**	**44**

Commercial

A provision was recognised in 2007 in relation to the cost of rectifying several billing application configuration issues primarily relating to prior periods. The provision covers the cost of investigating and resolving these issues.

Restructuring

A provision for restructuring costs was recognised in 2007 in relation to restructuring activities undertaken or announced in 2007, including a company-wide organisational redesign programme, the costs of rationalising Australian call centre operations, the integration of PowerTel Limited and costs relating to the cost of restructuring Telecom's information systems to separate Yellow Pages Group. The majority of the provision at 30 June 2008 relates to Yellow Pages Group, which is a discontinued operation. The restructuring is expected to be completed by the end of calendar year 2008.

Other

Other provisions relate to leasehold property decommissioning liabilities and legal provisions and are expected to be utilised by the year ended 30 June 2012.

Note 20 Debt due within one year

	GROUP		PARENT	
30 JUNE	2008	2007	2008	2007
(DOLLARS IN MILLIONS)	NZ$M	NZ$M	NZ$M	NZ$M
Long-term debt maturing within one year (see note 22)	559	201	-	-
Short-term debt	399	287	-	-
Due to subsidiaries	-	-	5,764	4,993
	958	**488**	**5,764**	**4,993**

None of Telecom's debt is secured and all rank pari passu with other liabilities.

Note 21 Long-term derivative liabilities

	GROUP	
30 JUNE	2008	2007
(DOLLARS IN MILLIONS)	NZ$M	NZ$M
Cross currency interest rate swaps	364	574
Interest rate swaps	3	1
Electricity price hedges	-	2
	367	**577**

Note 22 Long-term debt

	GROUP		PARENT	
30 JUNE	2008	2007	2008	2007
(DOLLARS IN MILLIONS)	NZ$M	NZ$M	NZ$M	NZ$M
Euro Medium Term Notes	1,952	1,921	-	-
Capital Notes	-	138	-	-
Telebonds	448	511	-	-
Other	-	49	2,846	2,442
	2,400	2,619	2,846	2,442
Less unamortised discount	(11)	(14)	-	-
	2,389	2,605	2,846	2,442
Less long-term debt maturing within one year (see note 20)	(559)	(201)	-	-
	1,830	**2,404**	**2,846**	**2,442**
Schedule of Maturities				
Due 1 to 2 years	15	553		
Due 2 to 3 years	14	64		
Due 3 to 4 years	328	14		
Due 4 to 5 years	249	324		
Due over 5 years	1,224	1,449		
Total due after one year	**1,830**	**2,404**		

None of Telecom's debt is secured and all ranks pari passu with other liabilities.

Euro medium term notes

30 JUNE (DOLLARS IN MILLIONS)			GROUP 2008	2007
INTEREST RATE	DUE	FACE VALUE	NZ$M	NZ$M
6.125%	12 Dec 2008	200m GBP	523	521
2.0%	8 June 2009	2bn JPY	25	21
6.75%	14 Dec 2011	250m USD	328	325
4.89%	11 Oct 2013	275m CAD	357	337
5.625%	14 May 2018	125m GBP	327	326
5.75%	6 April 2020	150m GBP	392	391
			1,952	**1,921**

Cross currency and interest rate swaps have been entered into to manage the Euro Medium Term Notes currency and interest rate risk exposures. See note 26.

Two of Telecom's existing Euro Medium Term Notes issues (a GBP200 million issue maturing December 2008 and a US$250 million issue maturing December 2011) have pricing triggers in the event of a rating downgrade. These triggers would require Telecom's long-term ratings from Standard & Poor's/Moody's Investor Services to fall below A-/A3 before increased interest rates would apply.

In August 2008 Telecom issued bonds maturing on the 6 August 2012 with a face value of CHF200 million, converted to NZ$258 million. See note 34.

Capital notes

30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	2007 NZ$M
Restricted capital securities	-	138
	-	**138**

Restricted capital securities

In February 1998 Telecom issued to certain qualified institutional buyers in the United States, under an Offering Memorandum pursuant to US SEC Rule 144A, an aggregate principal amount of face value US$150 million 6.5% Restricted capital securities for an initial term of ten years. The Restricted capital securities were repaid in full, in cash in February 2008.

TeleBonds

Telecom has issued bonds (TeleBonds) to institutional and retail investors. These have been issued as income, compounding, or zero coupon bonds. TeleBonds have interest rates ranging from 6.92% to 8.65% and maturity dates between September 2008 and April 2016. During 2006 Telecom completed a NZ$400 million TeleBond issue. The TeleBonds were issued in two tranches, NZ$250 million seven-year bonds and NZ$150 million ten-year bonds, with effective rates of 7.04% and 7.14% respectively.

In July and August 2008 Telecom issued NZ$142 million of Telebonds. See note 34.

Other long-term debt

Telecom acquired PowerTel in May 2007. PowerTel had existing loan facilities of A$55 million. No amounts were outstanding as at 30 June 2008 (30 June 2007: A$44 million).

Parent company

Amounts owing by the Parent are under a guarantee and payable to subsidiaries. There are no fixed repayment dates and amounts are not interest bearing.

Note 23 Equity

GROUP 30 JUNE (DOLLARS IN MILLIONS)	CONTRIBUTED CAPITAL NZ$M	RETAINED EARNINGS NZ$M	HEDGE RESERVE NZ$M	MINORITY INTEREST NZ$M	DEFERRED COMPENSATION NZ$M	REVALUATION RESERVE NZ$M	FOREIGN CURRENCY TRANSLATION RESERVE NZ$M	TOTAL EQUITY NZ$M
Balance at 30 June 2006	2,011	(960)	(36)	7	24	-	16	1,062
Translation of foreign operations	-	-	-	-	-	-	(120)	(120)
Hedge of net investment	-	-	-	-	-	-	38	38
Revaluation of investments	-	-	-	-	-	11	-	11
Cash flow hedges	-	-	(8)	-	-	-	-	(8)
Total (expense)/income recognised in equity	-	-	(8)	-	-	11	(82)	(79)
Net earnings for the year	-	3,024	-	3	-	-	-	3,027
Total recognised income and expenses	-	3,024	(8)	3	-	11	(82)	2,948
Dividends	-	(735)	-	(4)	-	-	-	(739)
Tax credit on supplementary dividends	-	83	-	-	-	-	-	83
Dividend reinvestment plan	249	-	-	-	-	-	-	249
Exercise of share options	1	-	-	-	-	-	-	1
Issuance of shares under share schemes	9	-	-	-	(9)	-	-	-
Balance at 30 June 2007	**2,270**	**1,412**	**(44)**	**6**	**15**	**11**	**(66)**	**3,604**
Translation of foreign operations	-	-	-	-	-	-	103	103
Hedge of net investment	-	-	-	-	-	-	(70)	(70)
Revaluation of investments	-	-	-	-	-	(11)	-	(11)
Cash flow hedges	-	-	51	-	-	-	-	51
Total income/(expense) recognised in equity	-	-	51	-	-	(11)	33	73
Net earnings for the year	-	710	-	3	-	-	-	713
Total recognised income and expenses	-	710	51	3	-	(11)	33	786
Dividends	-	(760)	-	(2)	-	-	-	(762)
Tax credit on supplementary dividends	-	85	-	-	-	-	-	85
Dividend reinvestment plan	195	-	-	-	-	-	-	195
Repurchase of shares	(65)	-	-	-	-	-	-	(65)
Issuance of shares under share schemes	10	-	-	-	(4)	-	-	6
Capital reduction	(1,113)	-	-	-	-	-	-	(1,113)
Balance at 30 June 2008	**1,297**	**1,447**	**7**	**7**	**11**	**0**	**(33)**	**2,736**

PARENT 30 JUNE (DOLLARS IN MILLIONS)	CONTRIBUTED CAPITAL NZ$M	RETAINED EARNINGS NZ$M	DEFERRED COMPENSATION NZ$M	TOTAL EQUITY NZ$M
Balance at 1 July 2006	2,011	(1,356)	24	679
Net earnings for the year	-	2,656	-	2,656
Total recognised income and expenses	-	2,656	-	2,656
Dividends	-	(735)	-	(735)
Tax credit on supplementary dividends	-	83	-	83
Dividend reinvestment plan	249	-	-	249
Exercise of share options	1	-	-	1
Issuance of shares under share schemes	9	-	(9)	-
Balance at 30 June 2007	**2,270**	**648**	**15**	**2,933**
Net earnings for the year	-	40	-	40
Total recognised income and expenses	-	40	-	40
Dividends	-	(760)	-	(760)
Tax credit on supplementary dividends	-	85	-	85
Dividend reinvestment plan	195	-	-	195
Issuance of shares under share schemes	10	-	(4)	6
Repurchase of shares	(65)	-	-	(65)
Capital reduction	(1,113)	-	-	(1,113)
Balance at 30 June 2008	**1,297**	**13**	**11**	**1,321**

Contributed capital

Movements in the Company's issued ordinary shares were as follows:

30 JUNE (DOLLARS IN MILLIONS)	2008 NUMBER	2008 NZ$M	2007 NUMBER	2007 NZ$M
Shares at the beginning of the year	2,019,993,131	2,270	1,960,933,948	2,011
Shares issued under the dividend reinvestment plan	48,176,233	195	56,809,102	249
Shares repurchased and cancelled	(244,116,062)	(1,178)	-	-
Shares issued under the restricted share scheme	967,894	7	1,534,186	4
Shares issued under the share rights scheme	647,077	2	486,888	2
Shares issued upon exercise of options	39,638	1	180,849	4
Other issues	-	-	48,158	-
Shares at the end of the year	1,825,707,911	1,297	2,019,993,131	2,270

All issued shares are fully paid and have no par value.

Each of the ordinary shares confers on the holder the right to vote at any general meeting of the Company except that the Company's constitution provides for certain restrictions on voting, including where a holder holds more than 10% of the ordinary shares in breach of shareholding limitations.

A special rights convertible preference share (the 'Kiwi Share') was created on 11 September 1990 and is registered in the name of, and may only be held by, the Minister of Finance on behalf of the Crown. The consent of the holder of the Kiwi Share is required for the amendment, removal or alteration of the effect of certain provisions of the Company's constitution which was adopted upon re-registration on 27 September 1996 under the Companies Act 1993.

The Company's constitution also contains provisions that require Telecom to observe certain principles relating to the provision of telephone services and their prices, and that require the consent of the holder of the Kiwi Share and the board of Telecom for a person to become the holder of an interest in 10% or more of the voting shares in Telecom.

The holder of the Kiwi Share is not entitled to vote at any meetings of the Company's shareholders nor participate in the capital or profits of the Company, except for repayment of NZ$1 of capital upon a winding up. The Kiwi Share may be converted to an ordinary share at any time by the holder thereof, at which time all rights and powers attached to the Kiwi Share will cease to have any application.

Capital repurchase

Following the sale of Yellow Pages Group in April 2007 for NZ$2.2 billion, Telecom announced on 3 May 2007 its intention to make a capital return to shareholders of approximately NZ$1.1 billion via a shareholder and court-approved scheme of arrangement. Under the scheme of arrangement, one in nine ordinary shares were cancelled on a pro-rata basis in exchange for NZ$4.88 for each cancelled share. The scheme of arrangement was approved by shareholders at a special meeting on 17 August 2007 and final High Court approval was obtained on 3 September 2007. The capital return was successfully completed in October 2007.

Australian shareholders received approximately A$4.17 per cancelled share.

Immediately following the capital return the ratio of ADRs to ordinary shares was changed from 1 ADR to 8 ordinary shares to 1 ADR to 5 ordinary shares. From an ADR holder's perspective the combination of the capital return and ratio change resulted in the receipt of approximately US$3.27 for every existing ADR held and the issue of 42.2% more ADRs.

In the view of the Telecom board, the NZ$1.1 billion capital return provided sufficient flexibility to accommodate any deterioration in the operating outlook and a significant ongoing capital expenditure programme.

Shares issued in lieu of dividends

Telecom established a dividend reinvestment plan effective from the third quarter of the year ended 30 June 2000. Under the plan, shareholders can elect to receive dividends in cash or additional shares. In respect of the year ended 30 June 2008, 48,176,233 shares with a total value of NZ$195 million were issued in lieu of a cash dividend (30 June 2007: 56,809,102 shares with a total value of NZ$249 million). To offset shares issued under the dividend reinvestment plan in the year ended 30 June 2008, a total of 16,065,971 shares with a market value of NZ$65 million were repurchased and cancelled (30 June 2007: nil).

Shares held in trust

As detailed in note 24, shares are held in Trust when they are waiting to be allocated to employees under the Telecom restricted share scheme. At 30 June 2008 199,482 shares were held in Trust (30 June 2007: 269,125).

Hedge reserve

Movements in the fair value portion of derivatives are recognised directly in the hedge reserve when that derivative is in an effective cash flow hedge relationship. Cash flow hedge relationships are established at the point the derivative is recognised by Telecom and documentation details the relationship and how effectiveness will be measured. The fair value of derivatives is removed from the hedge reserve and recognised in the carrying value of the hedged item or recognised in the income statement as appropriate.

Deferred compensation

Deferred compensation is recognised upon issue of a restricted share under the Telecom restricted share scheme or over the life of an option issued under the Telecom share rights scheme or Telecom share option scheme. Amounts are transferred to share capital upon the vesting of the share or the option.

Foreign currency translation reserve

Translation differences arising on the re-translation of the results and net assets of subsidiaries with functional currencies other than New Zealand dollars are recognised directly in the foreign currency translation reserve. Movements in the fair value of derivative financial instruments that are effective hedges of Telecom's net investment in subsidiaries subject to these translation differences are also recognised directly in the foreign currency translation reserve. The cumulative amounts are released to the income statement upon disposal of these subsidiaries.

Earnings per share

	GROUP		
YEAR ENDED 30 JUNE	2008	2007	2006
Basic earnings per share			
Numerator - Net earnings/(loss) from continuing operations (NZ$m)	713	844	(540)
Numerator - Net earnings from discontinued operations (NZ$m)	-	2,183	109
Numerator - Net earnings/(loss) attributable to equity holders (NZ$m)	710	3,024	(435)
Denominator - weighted average ordinary shares (in millions)	1,871	1,990	1,960
Basic earnings/(loss) per share (in dollars):			
From continuing operations[1]	NZ$.038	NZ$0.42	NZ$(0.28)
From discontinued operation	-	NZ$1.10	NZ$0.06
From net earnings/(loss) attributable to equity holders	NZ$0.38	NZ$1.52	NZ$(0.22)
Diluted earnings per share			
Numerator - as noted above adjusted by:			
Add - capital notes interest after income tax (NZ$m)	-	6	-
Denominator (in millions)			
Ordinary shares	1,871	1,990	1,960
Capital notes	-	34	-
Options	2	2	-
	1,873	2,026	1,960
Diluted earnings/(loss) per share (in dollars):			
From continuing operations[1]	NZ$0.38	NZ$0.42	NZ$(0.28)
From discontinued operation	-	NZ$1.08	NZ$0.06
From net earnings/(loss) attributable to equity holders	NZ$0.38	NZ$1.50	NZ$(0.22)
Anti-dilutive potential shares (in millions)			
Capital notes	-	-	89
Options	16	21	25

1 Earnings/(loss) per share from continuing operations is calculated after deducting minority interest.

Note 24 Employee share schemes

Telecom incentive schemes

Telecom has operated a share option scheme since 1994. During the year ended 30 June 2002, Telecom also established the Telecom restricted share scheme and Telecom share rights scheme. The total charge recognised for the schemes during the year was NZ$8 million (30 June 2007: NZ$12 million).

Telecom share option scheme

Telecom has operated a share option scheme since 1994 whereby certain key executives are granted a number of options to purchase ordinary shares in the Company. During the year ended 30 June 2002 the scheme was expanded to give both key executives and senior employees the option to participate in the scheme. The number of participants has subsequently been reduced from September 2003, with most employees now participating in the restricted share scheme. Each option granted will convert to one ordinary share on exercise. A participant may exercise his or her options (subject to employment conditions) any time during a prescribed period commencing at least one year from the date on which the options are conferred. A performance hurdle must be met in order to exercise any share options. The total return to shareholders, measured as the combination of share price appreciation and dividends paid, must exceed the estimated cost of equity since the grant of the share option. External advisors calculate the cost of equity annually and achievement of the performance hurdle is independently verified. Certain issues of options require total shareholders' return to exceed the return of similar telecommunications companies.

No options were issued to employees under the share option scheme during the years ended 30 June 2008 and 30 June 2007.

In prior years, options have been issued with a maximum term of six years. New ordinary shares will be issued in accordance with the constitution upon the exercise of options. The price payable on exercise will be equivalent to the average daily closing price of Telecom shares reported on the New Zealand Stock Exchange for the business days in the month immediately preceding the date on which options are granted (subject to adjustment if the shares traded 'cum dividend'). The options granted are determined by a committee of the board of directors pursuant to the share option scheme. The weighted average grant date fair value of options issued during 2006 was NZ$0.67. The average share price during the year was NZ$4.14 (30 June 2007: NZ$4.57) and the intrinsic value of options exercised was nil (30 June 2007: nil). The intrinsic value of options outstanding and exercisable as at 30 June 2008 is nil (30 June 2007: nil).

Information regarding options granted under the share option scheme is as follows:

	OPTION PRICE[1] NZ$	NUMBER OF OPTIONS
As at 30 June 2006	5.46	23,256,544
Granted	-	-
Exercised	4.79	(180,849)
Forfeited	6.09	(328,059)
Lapsed	6.07	(3,949,736)
As at 30 June 2007	5.33	18,797,900
Granted	-	-
Exercised	4.70	(39,638)
Forfeited	6.11	(671,003)
Lapsed	4.99	(5,175,129)
As at 30 June 2008	**5.42**	**12,912,130**

1 Weighted average

	OPTIONS OUTSTANDING				OPTIONS CURRENTLY EXERCISABLE	
PERIOD GRANTED	OPTIONS OUTSTANDING	PRICE RANGE NZ$	PRICE[1] NZ$	REMAINING LIFE[1] (YEARS)	OPTIONS EXERCISABLE	PRICE[1] NZ$
1 July 2002 – 30 June 2003	4,406,345	4.43 – 4.94	4.93	0.2	4,406,345	4.93
1 July 2003 – 30 June 2004	2,777,943	5.01	5.01	1.2	2,777,973	5.01
1 July 2004 – 30 June 2005	3,606,006	5.93 – 6.30	5.95	2.2	3,606,006	5.95
1 July 2005 – 30 June 2006	2,121,836	6.11	6.11	3.2	898,981	6.11
	12,912,130				**11,689,275**	

1 Weighted average

	OPTIONS OUTSTANDING			OPTIONS CURRENTLY EXERCISABLE	
PRICE RANGE	OPTIONS OUTSTANDING	PRICE[1] NZ$	REMAINING LIFE[1] (YEARS)	OPTIONS EXERCISABLE	PRICE[1] NZ$
4.00 – 4.99	4,406,345	4.93	0.2	4,406,345	4.93
5.00 – 5.99	6,363,711	5.54	1.8	6,363,711	5.54
6.00 – 6.99	2,142,074	6.11	3.2	919,219	6.11
	12,912,130			**11,689,275**	

1 Weighted average

Telecom restricted share scheme

In September 2001 the Telecom restricted share scheme ('RSS') was introduced for selected executives and senior employees of the group. In September 2003 participation was extended so that the majority of employees who previously participated in the share options scheme participated in the RSS. Under the RSS, Company shares are issued to Telecom Trustee Limited, a Telecom subsidiary and allocated to participants using funds lent to them by the Company. Under the RSS, the length of the retention period before awards vest is between one to three years. The price for each share issued during the year under the RSS is the average end-of-day market price of Telecom shares reported on the New Zealand Stock Exchange for the days on which the exchange is open for trading in the month immediately preceding the date on which the share is allocated, adjusted for dividends that are not received until the share vests. If the individual is still employed by the group at the end of the specified period, the employee is given a cash bonus which must be used to repay the loan and the restrictions on the shares are removed. The number of shares awarded is determined by a committee of the board of directors. The weighted average grant date fair value of restricted shares issued during the year was NZ$4.29 (30 June 2007: NZ$3.52). Shares with a grant date fair value of NZ$5 million vested during the year (30 June 2007: NZ$4 million).

Information regarding shares awarded under the RSS is as follows:

	NUMBER OF SHARES
Unvested shares as at 30 June 2006	2,465,897
Awarded pursuant to RSS	1,841,278
Forfeited	(561,694)
Vested	(817,041)
Unvested shares as at 30 June 2007	2,928,440
Awarded pursuant to RSS	1,435,702
Forfeited	(382,647)
Cancelled	(240,650)
Vested	(747,508)
Unvested shares as at 30 June 2008	2,993,337
Percentage of total ordinary shares	0.16%

The number of shares awarded pursuant to the RSS does not equal the number of shares created for the scheme as lapsed shares are held in Trust and reissued.

Telecom share rights scheme

The Telecom Share Rights Scheme ('SRS') was introduced for selected executives and senior employees of the group in September 2001. Under the scheme, participants are granted the option to purchase Company shares at a nil exercise price. Under the SRS, the exercise date of each option is variable, but in the main is three years from the allocation date. Except under special circumstances, the options will be exercisable at the end of a specified period only if the individual is still employed by the group. The number of options granted is determined by a committee of the board of directors. The weighted average grant date fair value of options issued during the year was NZ$3.80 (30 June 2007: NZ$3.42). The intrinsic value of options exercised during the year was NZ$3 million (30 June 2007: NZ$2 million). Options with an intrinsic value of NZ$7 million remain outstanding at the year end.

Information regarding options granted under the SRS is as follows:

	NUMBER OF OPTIONS
As at 30 June 2006	1,674,033
Granted	1,178,208
Exercised	(486,888)
Forfeited	(421,251)
As at 30 June 2007	1,944,102
Granted	1,362,104
Exercised	(647,077)
Cancelled	(172,780)
Forfeited	(466,957)
As at 30 June 2008	2,019,392

PERIOD GRANTED	OPTIONS OUTSTANDING	REMAINING LIFE[1] (YEARS)
1 July 2004 – 30 June 2005	2,452	0.1
1 July 2005 – 30 June 2006	331,738	0.5
1 July 2006 – 30 June 2007	478,568	1.2
1 July 2007 – 30 June 2008	1,206,634	2.4
	2,019,392	

1 Weighted average

2,452 options were exercisable as at 30 June 2008.

Fair value of share scheme awards

The fair value of share options issued in prior years was estimated using a lattice-binomial option pricing model. The model was based on the following weighted average assumptions:

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS)	GROUP 2006
Risk-free interest rate	5.6%
Expected dividend yield	6.6%
Expected option life (in years)	4.2
Expected stock price volatility	21.0%

Risk-free interest rates were between 5.6% - 5.7% and the expected dividend yields were between 6.6% - 8.5%. The contractual term of options and employees' expected exercise behaviour is calculated based on historical data. The discount applied for post vesting restrictions is estimated using the probability of those restrictions impacting the exercise of options. Approximately NZ$13 million of share scheme awards remain unvested and not expensed as at 30 June 2008 (30 June 2007: NZ$14 million). This expense will be recognised over the vesting period of the awards to 30 June 2011.

Restricted shares and options granted under the share rights scheme are valued based on the market price at grant date, adjusted if dividends are not received until the restricted share or option vests. Volatility is based on historic volatility in Telecom's share price.

Note 25 Dividends

Dividends declared and provided by the Company are as follows:

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS, EXCEPT FOR PER SHARE AMOUNTS)	2008 NZ$M	2007 NZ$M
Previous year fourth quarter dividend paid	292	235
Supplementary dividend	36	30
First quarter dividend paid	128	139
Supplementary dividend	16	17
Second quarter dividend paid	128	139
Supplementary dividend	16	18
Third quarter dividend paid	128	139
Supplementary dividend	16	18
	760	**735**
Fourth quarter dividend declared subsequent to balance date not provided for (see note 34)	146	292
Dividends per share (including dividends paid during the year but excluding supplementary dividends)	NZ$0.355	NZ$0.33

Telecom receives an equivalent tax credit from the Inland Revenue Department for the amount of supplementary dividends paid.

The following summary is based on tax laws of New Zealand as at 30 June 2008 and is subject to changes in New Zealand tax law, including changes that could have retroactive effect. Shareholders should seek taxation advice on the taxation treatment of their dividends.

In general, shareholders may be subject to income tax on dividends received from Telecom under the relevant taxation laws to which they are subject.

Generally, to the extent imputation credits are attached to dividends, New Zealand tax resident shareholders may be able to claim the imputation credits to reduce their New Zealand income tax liability on any gross dividend amount. To the extent dividends are imputed at a rate of less than 33/67, resident withholding tax will be deducted (at a maximum rate of 33%) from dividend payments made to New Zealand tax resident shareholders.

New Zealand generally imposes a 30% withholding tax on dividends paid by a New Zealand company to a non-resident shareholder. However, to the extent to which dividends have maximum imputation credits attached the rate of withholding is 15%. Also, reduced rates (generally 15% at the maximum rate allowed) apply to non-resident shareholders who are entitled to the benefit of an income tax treaty. To the extent imputation credits are attached to dividends a supplementary dividend (which is in addition to an ordinary dividend) may be attached to dividends to non-resident shareholders to offset the rate of withholding.

Shares issued in lieu of dividends

Telecom established a dividend reinvestment plan effective from the third quarter of the year ended 30 June 2000. Under the plan shareholders can elect to receive dividends in cash or additional shares. In respect of the year ended 30 June 2008, 48,176,233 shares with a total value of NZ$195 million were issued in lieu of a cash dividend (30 June 2007: 56,809,102 shares and NZ$249 million). Shares issued in lieu of dividends are excluded from dividends paid in the cash flow statement.

Note 26 Financial instruments and risk management

Telecom manages its treasury activities through a board-approved treasury constitution consisting of treasury governance and policy frameworks. Telecom is exposed to foreign currency, interest rate, credit, liquidity, equity and electricity price risks. Each of these risks, the associated financial instruments and the management of those risks are detailed below.

Telecom's financial instruments are classified under NZ IFRS as follows:

GROUP AS AT 30 JUNE 2008 (DOLLARS IN MILLIONS)	HELD-FOR-TRADING NZ$M	AVAILABLE-FOR-SALE NZ$M	LOANS AND RECEIVABLES NZ$M	HELD TO MATURITY NZ$M	DESIGNATED IN HEDGING RELATIONSHIPS NZ$M	AMORTISED COST NZ$M	TOTAL CARRYING AMOUNT NZ$M
Assets							
Current assets							
Cash	-	-	-	779	-	-	779
Short-term derivative assets	2	-	-	-	13	-	15
Trade receivables	-	-	498	-	-	-	498
	2	**-**	**498**	**779**	**13**	**-**	**1,292**
Non-current assets							
Long-term derivative assets	-	-	-	-	48	-	48
Long-term investments[1]	-	523	-	1	-	-	524
	-	**523**	**-**	**1**	**48**	**-**	**572**
Liabilities							
Current liabilities							
Short-term derivative liabilities	-	-	-	-	(214)	-	(214)
Trade accounts payable	-	-	-	-	-	(780)	(780)
Short-term debt	-	-	-	-	-	(399)	(399)
Long-term debt due within one year	-	-	-	-	-	(559)	(559)
	-	**-**	**-**	**-**	**(214)**	**(1,738)**	**(1,952)**
Non-current liabilities							
Long-term derivative liabilities	(64)	-	-	-	(303)	-	(367)
Long-term debt due after one year	-	-	-	-	-	(1,830)	(1,830)
	(64)	**-**	**-**	**-**	**(303)**	**(1,830)**	**(2,197)**

1 Excludes associates

GROUP AS AT 30 JUNE 2007 (DOLLARS IN MILLIONS)	HELD-FOR-TRADING NZ$M	AVAILABLE-FOR-SALE NZ$M	LOANS AND RECEIVABLES NZ$M	HELD TO MATURITY NZ$M	DESIGNATED IN HEDGE RELATIONSHIP NZ$M	AMORTISED COST NZ$M	TOTAL CARRYING AMOUNT NZ$M
Assets							
Current assets							
Cash	-	-	-	1,969	-	-	1,969
Short-term investments	-	-	-	70	-	-	70
Short-term derivative assets	-	-	-	-	8	-	8
Trade receivables	-	-	544	-	-	-	544
	-	**-**	**544**	**2,039**	**8**	**-**	**2,591**
Non -current assets							
Long-term derivative assets	-	-	-	-	68	-	68
Long-term investments [1]	-	490	-	1	-	-	491
	-	**490**	**-**	**1**	**68**	**-**	**559**
Liabilities							
Current liabilities							
Short-term derivative liabilities	-	-	-	-	(68)	-	(68)
Trade accounts payable	-	-	-	-	-	(708)	(708)
Short-term debt	-	-	-	-	-	(287)	(287)
Long-term debt due within one year	-	-	-	-	-	(201)	(201)
	-	**-**	**-**	**-**	**(68)**	**(1,196)**	**(1,264)**
Non-current liabilities							
Long-term derivative liabilities	(51)	-	-	-	(526)	-	(577)
Long-term debt due after one year	-	-	-	-	-	(2,404)	(2,404)
	(51)	**-**	**-**	**-**	**(526)**	**(2,404)**	**(2,981)**

1 excludes associates

Telecom uses derivative financial instruments to reduce its exposure to fluctuations in foreign currency exchange rates, interest rates and electricity prices. The notional values of contract amounts outstanding are as follows:

30 June (dollars in millions)	Currency	Maturities	Group 2008 NZ$M	Group 2007 NZ$M
Cross currency interest rate swaps	AUD:USD	2011	610	533
	NZD:GBP	2008-2020	1,426	1,426
	NZD:JPY	2009	41	41
	NZD:USD	2008	-	181
	NZD:CAD	2013	378	378
Interest rate swaps	AUD	2011	472	411
	NZD	2008-2020	2,182	2,362
Forward exchange contracts	NZD:AUD	2008	351	333
	NZD:USD	2008-2009	169	248
	NZD:DKK	2008	714	-
	Other	2008-2009	75	29
Currency options	NZD:USD	2008-2009	86	121
	Other	2008	38	34

Reclassifications

There have been no reclassifications between financial instrument categories during the year ended 30 June 2008.

Fair value of financial instruments

Financial instruments are either carried at amortised cost, less any provision for impairment, or fair value. The only significant variances between amortised cost and fair value relate to long-term debt.

The fair value of long-term debt is NZ$2,353 million compared to a carrying value of NZ$2,389 million (30 June 2007: fair value of NZ$2,622 million compared to a carrying value of NZ$2,605 million). Long-term investments, excluding associates, are carried at NZ$524 million (30 June 2007: NZ$491 million) and consisted of investments in equity. At 30 June 2008 NZ$449 million of the long-term investments related to Hutchison Telecommunications (Australia) Limited ('HTAL') (30 June 2007: NZ$416 million in Hutchison 3G Australia Limited). Telecom's investment is difficult to value given the fact that this business is still in an early stage in its life cycle and continues on a period of rapid growth as the business attempts to achieve the scale required to generate a satisfactory return on its equity in the long run. HTAL is quoted on the Australian Stock Exchange, however Telecom considers that is not an active market for the shares of HTAL and that the share price does not represent the fair value of the investment in HTAL. As at 30 June 2008 the quoted price of HTAL's shares on the Australian Stock Exchange is A$0.10 and Telecom's carrying value per share equates to A$0.26. Telecom considers that there is no objective measure of fair value and the wide range of estimates of fair value that exists is due to the level of uncertainty surrounding Hutchison's future cash flows. Given the lack of a reliable fair value, Telecom continues to hold its investment in Hutchison at cost and therefore cannnot disclose a fair value.

The following methods and assumptions were used to estimate the fair value of each class of financial instrument:

Cash, short-term investments, debt due within one year, trade receivables and trade accounts payable

The carrying amounts of these balances are approximately equivalent to their fair value because of the short term to maturity.

Long-term investments

At 30 June 2008 Telecom had quoted and unquoted investments. The quoted investments have standard terms and conditions and are traded on an active market. Their fair values are based on their bid price, except for HTAL as noted above. Telecom considers that there are no reliable fair values for Telecom's unquoted investments.

Long-term debt

The fair value of long-term debt is calculated based on market prices for interest rate swaps with similar maturities, plus a credit margin to reflect the rates available to Telecom for similar debt securities.

Cross currency interest rate swaps, interest rate swaps, forward exchange contracts and currency options

The fair values are estimated on the basis of the quoted market prices of these instruments. If a listed market price is unavailable, then a fair value is estimated by using a valuation model involving discounted future cash flows of the derivative using applicable forward price curve (for the relevant interest rate, foreign exchange rate or commodity price) and discount rates.

Market risk

Telecom is exposed to market risk primarily from changes in foreign currency exchange rates and interest rates.

Telecom employs risk management strategies including the use of derivatives such as interest rate swaps, foreign currency forwards, foreign currency options, and cross currency interest rate swaps to manage these exposures. Telecom monitors the use of derivative financial instruments through the use of well-defined market and credit risk limits and timely reports to senior management. Telecom does not hold or issue derivative financial instruments for trading purposes. All contracts have been entered into with major creditworthy financial institutions, and the risk associated with these transactions is the cost of replacing these agreements at the current market rates in the event of default by the counterparts. Telecom's financial instruments do not have significant concentration of risk with any single party.

Currency risk

Telecom's primary objective in managing foreign currency risk is to protect against the risk that the eventual New Zealand dollar net cash flows will be adversely affected by changes in foreign currency exchange rates. To do this Telecom enters into forward exchange contracts to reduce its foreign currency exposures. Forward exchange contracts are also used to hedge certain foreign currency assets.

Foreign currency assets, where appropriate are naturally hedged by holding liabilities in the same currency. Capital and operational expenditure in foreign currencies that are probable may be hedged. Exposures with amounts and timing that are less than certain can be proportionately hedged, based on certain benchmarks.

The majority of Telecom's long-term debt has been issued in foreign currencies. Telecom enters into cross currency interest rate swaps to convert issue proceeds into a floating rate New Zealand dollar, or Australian dollar exposure. All debt not denominated in New Zealand dollars or Australian dollars is fully hedged. Debt denominated in foreign currencies is translated to New Zealand dollars with gains, or losses going to the income statement. These gains, or losses are offset by the translation of the principal value of the cross currency interest rate swaps.

As at 30 June 2008 Telecom has NZ$487 million of deposits denominated in Danish krone, which are hedged by forward exchange contracts.

Telecom uses foreign currency forwards and foreign currency options to hedge forecast transactions that have a high probability of occurrence and firm purchase commitments (mainly denominated in US dollars), fair value changes in foreign currency receivables and payables and to hedge its net investments in foreign operations.

Telecom's exposure to foreign currencies arising from financial instruments is:

GROUP AS AT 30 JUNE 2008 (DOLLARS IN MILLIONS)	AUD NZ$M	USD NZ$M	EUR NZ$M	GBP NZ$M	CAD NZ$M	DKK NZ$M	OTHER NZ$M	TOTAL NZ$M
Exposures								
Cash	37	15	-	31	-	487	2	572
Trade receivables	171	29	-	16	3	-	2	221
Trade accounts payables	(177)	(114)	(7)	(25)	(3)	-	(2)	(328)
Long-term investments	51	-	-	-	-	-	-	51
Short-term debt	(155)	(39)	-	-	-	-	-	(194)
Long-term debt	-	(325)	-	(1,238)	(356)	-	(25)	(1,944)
Net balance sheet exposure	**(73)**	**(434)**	**(7)**	**(1,216)**	**(356)**	**487**	**(23)**	**(1,622)**
Hedging instruments								
Forward exchange contracts	(371)	172	73	-	-	(719)	7	(838)
NZ$ cross currency interest rate swaps	-	-	-	1,238	356	-	25	1,619
A$ cross currency interest rate swaps	(610)	325	-	-	-	-	-	(285)
Total hedging instruments	**(981)**	**497**	**73**	**1,238**	**356**	**(719)**	**32**	**496**

GROUP AS AT 30 JUNE 2007 (DOLLARS IN MILLIONS)	AUD NZ$M	USD NZ$M	EUR NZ$M	GBP NZ$M	CAD NZ$M	DKK NZ$M	OTHER NZ$M	TOTAL NZ$M
Exposures								
Cash	25	10	-	27	-	1	2	65
Trade receivables	160	73	3	3	7	-	2	248
Trade accounts payables	(161)	(131)	(5)	(1)	(7)	-	(2)	(307)
Long-term investments	51	-	-	-	-	399	-	450
Short-term debt	(287)	-	-	-	-	-	-	(287)
Long-term debt	(49)	(459)	-	(1,231)	(336)	-	(21)	(2,096)
Net balance sheet exposure	**(261)**	**(507)**	**(2)**	**(1,202)**	**(336)**	**400**	**(19)**	**(1,927)**
Hedging instruments								
Forward exchange contracts	(325)	225	8	1	-	-	14	(77)
NZ$ cross currency interest rate swaps	-	138	-	1,231	336	-	21	1,726
A$ cross currency interest rate swaps	(532)	321	-	-	-	-	-	(211)
Total hedging instruments	**(857)**	**684**	**8**	**1,232**	**336**	**-**	**35**	**1,438**

The table above includes Telecom's foreign currency exposures to financial instruments. Non-financial assets or liabilities of foreign operations are not included. Forecast sales and purchases in foreign currencies have not been included in the table above as they are not financial instruments.

The Danish krone deposits at 30 June 2008 are hedged on an after tax basis, hence on a pre-tax basis Telecom has an exposure to Danish krone.

As at 30 June 2008 a movement of 10% in the New Zealand dollar would impact the income statement and statement of changes in equity as detailed in the table below:

IMPACT ON:	NZ$M -10%	NZ$M +10%
Net profit before tax	8	(2)
Equity	(125)	103

This analysis assumes a movement in the New Zealand dollar across all currencies and only includes the effect of foreign exchange movements on financial instruments. All other variables remain constant.

Interest rate risk

Telecom employs the use of derivative financial instruments for the purpose of reducing its exposure to fluctuations in interest rates.

Telecom has used cross currency interest rate swaps to convert foreign currency borrowings into floating rate New Zealand dollar and Australian dollar exposure. Interest rate swaps have been used to convert the majority of this floating rate exposure into fixed rate exposure. As a consequence, Telecom's interest rate exposure is limited to New Zealand and Australian yield curves. The objectives of interest rate risk management are to minimise the cost of net borrowings and to minimise the impact of interest rate movements on Telecom's interest expense and net earnings within policies approved by the Telecom board.

Telecom's treasury constitution requires that interest rate repricing is to be spread over a 10 year horizon and a maximum of NZ$800 million or 20% of gross debt to be repriced in any financial year.

Repricing analysis

The following table indicates the effective interest rates and the earliest period in which recognised financial instruments reprice. These balances are presented including the effect of derivative financial instruments.

GROUP 30 JUNE 2008 (DOLLARS IN MILLIONS)	WEIGHTED EFFECTIVE INTEREST RATE	WITHIN 1 YEAR NZ$M	1-2 YEARS NZ$M	2-3 YEARS NZ$M	3-4 YEARS NZ$M	4-5 YEARS NZ$M	GREATER THAN 5 YEARS NZ$M	TOTAL NZ$M
Floating rate								
Cash balances	5.3%	779	-	-	-	-	-	779
Long-term debt	9.1%	(139)	-	-	-	-	-	(139)
Fixed rate								
Short-term debt	8.2%	(399)	-	-	-	-	-	(399)
Long-term debt	7.9%	(743)	(15)	(14)	(471)	(249)	(1,261)	(2,753)
		(502)	**(15)**	**(14)**	**(471)**	**(249)**	**(1,261)**	**(2,512)**

GROUP 30 JUNE 2007 (DOLLARS IN MILLIONS)	WEIGHTED EFFECTIVE INTEREST RATE	WITHIN 1 YEAR NZ$M	1-2 YEARS NZ$M	2-3 YEARS NZ$M	3-4 YEARS NZ$M	4-5 YEARS NZ$M	GREATER THAN 5 YEARS NZ$M	TOTAL NZ$M
Floating rate								
Cash balances	7.7%	1,969	-	-	-	-	-	1,969
Long-term debt	7.8%	(170)	-	-	-	-	-	(170)
Fixed rate								
Short-term investments	8.3%	70	-	-	-	-	-	70
Short-term debt	6.5%	(287)	-	-	-	-	-	(287)
Long-term debt	7.9%	(244)	(742)	(15)	(14)	(531)	(1,388)	(2,934)
		1,338	**(742)**	**(15)**	**(14)**	**(531)**	**(1,388)**	**(1,352)**

The table below shows how a movement in interest rates of 100 basis points would affect net profit before tax and equity based on the revaluation of Telecom's financial instruments as at 30 June 2008:

IMPACT ON:	-100BP NZ$M	+100BP NZ$M
Net profit before tax	2	(2)
Equity	(1)	2

This analysis assumes all other variables remain constant.

Liquidity risk

Liquidity risk represents Telecom's ability to meet its contractual obligations. Telecom evaluates its liquidity requirements on an ongoing basis. In general, Telecom generates sufficient cash flows from its operating activities to meet its financial liabilities.

In the event of any shortfalls, Telecom has three short-term financing programmes in place; a US$1 billion European Commercial Paper Programme, a NZ$500 million Note facility, and an A$1.5 billion Short Term Note and Medium Term Note Programme.

In addition to the short-term financing programmes at 30 June 2008, Telecom had committed stand-by facilities of NZ$800 million (30 June 2007 US$500 million) with a number of credit worthy banks. As at 30 June 2008 Telecom also had committed overdraft facilities of NZ$20 million with New Zealand banks and A$20 million with Australian banks. There are no compensating balance requirements associated with these facilities.

Telecom's liquidity policy is to maintain unutilised committed facilities or liquid resources (comprising cash and short-term investments) of 100% of the next 12 months' funding requirements. The policy also requires that long-term debt maturities are distributed over a 10-year period, with no more than NZ$800 million maturing in any one year. Long-term debt must have a weighted average life of between 3.75 and 5.25 years.

Telecom's maximum exposure to liquidity risk based on contractual cash flows relating to financial instruments is summarised below:

GROUP 30 JUNE 2008 (DOLLARS IN MILLIONS)	CARRYING AMOUNT NZ$M	CONTRACTUAL CASH FLOWS NZ$M	0-6 MONTHS NZ$M	6-12 MONTHS NZ$M	1-2 YEARS NZ$M	2-3 YEARS NZ$M	3-4 YEARS NZ$M	4-5 YEARS NZ$M	5+ YEARS NZ$M
Non-derivative financial liabilities									
Trade accounts payable	(780)	(780)	(780)	-	-	-	-	-	-
Short-term debt	(399)	(406)	(406)	-	-	-	-	-	-
Long-term debt	(2,389)	(3,248)	(611)	(93)	(123)	(124)	(439)	(337)	(1,521)
Derivative financial liabilities									
Interest rate swaps	(3)	(5)	-	-	1	-	(1)	(1)	(4)
Cross currency interest rate swaps	(551)	(1,046)	(222)	(49)	(82)	(82)	(337)	(49)	(225)
Foreign exchange contracts	(27)	(23)	(22)	(1)	-	-	-	-	-
	(4,149)	**(5,508)**	**(2,041)**	**(143)**	**(204)**	**(206)**	**(777)**	**(387)**	**(1,750)**

GROUP 30 JUNE 2007 (DOLLARS IN MILLIONS)	CARRYING AMOUNT NZ$M	CONTRACTUAL CASH FLOWS NZ$M	0-6 MONTHS NZ$M	6-12 MONTHS NZ$M	1-2 YEARS NZ$M	2-3 YEARS NZ$M	3-4 YEARS NZ$M	4-5 YEARS NZ$M	5+ YEARS NZ$M
Non-derivative financial liabilities									
Trade accounts payable	(708)	(708)	(708)	-	-	-	-	-	-
Short-term debt	(287)	(289)	(289)	-	-	-	-	-	-
Long-term debt	(2,605)	(3,566)	(84)	(272)	(696)	(124)	(124)	(435)	(1,831)
Derivative financial liabilities									
Interest rate swaps	(1)	-	6	(6)	-	-	-	-	-
Cross currency interest rate swaps	(617)	(1,154)	(50)	(108)	(272)	(77)	(78)	(261)	(308)
Foreign exchange contracts	(25)	(26)	(21)	(5)	-	-	-	-	-
Electricity price hedge	(2)	(3)	(1)	(1)	(1)	-	-	-	-
	(4,245)	**(5,746)**	**(1,147)**	**(392)**	**(969)**	**(201)**	**(202)**	**(696)**	**(2,139)**

Carrying amounts are as disclosed on the balance sheet as per Telecom's accounting policies. Contractual cash flows include contractual, undiscounted principal and interest payments.

Credit risk

In the normal course of its business, Telecom incurs credit risk from financial instruments including, cash, short-term investments, advances to associate companies, trade receivables and derivative financial instruments

Telecom has a credit policy that is used to manage this exposure to credit risk. As part of this policy, limits on exposures with counterparties have been set and approved by the board of directors and are monitored on a regular basis.

Telecom has certain derivative transactions that are subject to bilateral credit support agreements that require Telecom or the counterparty to post collateral to support mark-to-market valuation differences. As at 30 June 2008 Telecom had posted US$10 million (30 June 2007: US$14 million) of collateral in relation to various cross currency interest rate swaps. Additional margin calls can be made by either party if the fair value of the cross currency interest rate swaps changes due to market conditions.

Telecom places its cash, short-term investments and derivative financial instruments with high credit quality financial institutions and sovereign bodies and limits the amount of credit exposure to any one financial institution. These limits are monitored daily. There is no significant concentration of credit risk with respect to trade receivables.

NZ$1,847 million of Telecom's assets are subject to credit risk (30 June 2007: NZ$3,076 million). Telecom holds various letters of credit and guarantees over some of these amounts. Telecom does not hold any collateral over these amounts.

Telecom's trade receivables are aged as follows:

30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	2007 NZ$M
Current	204	331
0-30 Days past due	226	128
30-60 Days past due	53	30
60-90 Days past due	21	14
90+ Days past due	26	85
	530	**588**

Telecom has NZ$295 million (30 June 2007: NZ$213million) of financial assets that are overdue and not impaired.

Telecom maintains a provision for estimated losses expected to arise from customers being unable to make required payments. This provision takes into account known commercial factors impacting specific customer accounts, as well as the overall profile of Telecom's receivables portfolio. In assessing the provision, factors such as past collection history, the age of receivable balances, the level of activity in customer accounts, as well as general macro-economic trends, are taken into account. Significant changes in these factors would likely necessitate changes in the doubtful debts provision. At present, however, Telecom considers the current level of its allowance for doubtful accounts to be adequate to cover expected credit losses in its accounts receivable balances. Bad debt expenses are reported as other operating expenses in the income statement.

Movements in allowance for doubtful accounts are as follows:

30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	2007 NZ$M
Balance at beginning of period	44	39
Charged to costs and expenses	34	40
Bad debts recovered	(5)	(7)
Balance written off against provision	(41)	(28)
Balance at end of period	**32**	**44**

Electricity price risk

Telecom uses electricity hedges to reduce exposure to electricity spot price movements. At 30 June 2008, Telecom had contracts to hedge electricity consumption of 16 megawatts per hour (30 June 2007: 20 megawatts per hour) with maturity dates ranging from December 2008 to March 2009. A10% movement in electricity price would not have a significant effect on Telecom's earnings.

Equity risk

Investments that subject Telecom to equity risk include long-term investments in listed and unlisted companies as well as investment in associate companies. Telecom's exposure to equity risk at 30 June 2008 was NZ$527 million (30 June 2007: NZ$494 million). Telecom manages its exposure to equity risk through representation on the board of investee companies or through regular reviews of the investee's current and projected performance. A10% movement in quoted prices would increase or decrease Telecom's equity by NZ$5 million.

Hedging activities

Telecom is exposed to market risk primarily from changes in interest rates and foreign currency exchange rates. Telecom employs risk management strategies including the use of derivatives such as interest rate swaps, foreign currency forwards, foreign currency options, and cross currency interest rate swaps to manage these exposures.

Telecom does not currently hold or issue derivative financial instruments for trading purposes, although under the classifications of IFRS derivative financial instruments are classified as 'held for trading' unless they are designated hedges.

Each derivative which is designated as a hedge is classified as either:

- A hedge of the fair value of recognised assets or liabilities (a fair value hedge) or
- A hedge of a highly probable forecast transaction (a cash flow hedge) or
- A hedge of a net investment in foreign operations.

The fair values of derivatives in hedging relationships and held for trading are as follows:

30 June (dollars in millions)	Group 2008 Assets NZ$M	Group 2008 Liabilities NZ$M	Group 2007 Assets NZ$M	Group 2007 Liabilities NZ$M
Net Investment Hedges				
Foreign exchange forward contracts	-	(24)	7	-
	-	**(24)**	**7**	**-**
Cash flow hedges				
Foreign exchange forward contracts	9	(3)	-	(25)
Interest rate swaps	49	(3)	69	(1)
Cross currency interest rate swaps	-	(487)	-	(566)
Electricity price hedges	3	-	-	(2)
	61	**(493)**	**69**	**(594)**
Designated as held for trading				
Currency options	2	-	-	-
Cross currency interest rate swaps	-	(64)	-	(51)
	2	(64)	-	(51)
Total net derivative liabilities	**63**	**(581)**	**76**	**(645)**

Cash flow hedges

Telecom has converted the remainder of its fixed rate, foreign dollar denominated debt into New Zealand dollar and Australian dollar fixed rate debt using cross currency interest rate swaps and interest rate swaps. These swaps are jointly designated as hedges of the forecast interest and principal cash flows of the debt. The mark-to-market of the interest rate component of the swaps will enter into the determination of profit or loss over the life of the swaps designated cash flow hedges as follows:

30 June (dollars in millions)	Group 2008 NZ$M	Group 2007 NZ$M
Maturity:		
Less than 1 year	(3)	1
1 – 2 years	-	(12)
2 – 3 years	2	-
3 – 4 years	30	7
4 – 5 years	-	8
Maturity thereafter	(27)	(42)
	2	**(38)**

The fair value (of both interest rate and foreign exchange components) of the cash flow hedges is transferred to the income statement at the same time as the underlying hedged transaction affects the determination of income, which occurs upon the scheduled payment of interest and ultimate maturity of the debt. Telecom enters into foreign exchange contracts to hedge foreign currency purchases. The majority of the purchases are forecast to be made within 12 months of the balance sheet date.

Deferred gains or losses on hedge contracts will be included in the income statement at the same time as the underlying purchase impacts the determination of income. If the purchase relates to an operating expenditure item, the hedge gain or loss will be recognised when the underlying expense is recognised. If the purchase relates to an item of property, plant and equipment, the hedge gain or loss will be recognised in the income statement as the asset depreciates. If the purchase relates to an inventory item, the hedge gain or loss will be recognised in the income statement when the underlying inventory is expensed.

During the period there were no material hedged forecast transactions that were not expected to occur. There has been no ineffectiveness on cash flow hedging relationships during the year (30 June 2007: nil).

Net investment hedges

Net investment hedges relate to hedges of the effect of movements in foreign exchange rates on certain assets held in overseas subsidiaries. The effective portion of any gain or loss on hedges of net investments in foreign operations is recognised in equity and the gain or loss relating to any ineffective portion is recognised immediately in the income statement. Gains and losses included in equity are included in the income statement when the foreign operation is disposed of. There has been no ineffectiveness on net investment hedging relationships during the year (30 June 2007: nil).

Fair value hedge

As at 30 June 2008 and 30 June 2007, Telecom did not have any financial instruments in fair value hedge relationships.

Telecom has converted a portion of its fixed rate foreign dollar debt into a domestic floating rate exposure using a cross currency interest rate swap. This relationship was designated as a fair value hedge of the interest rate exposure. This hedge relationship became ineffective during the year ended June 2007 and Telecom has ceased hedge accounting. In the year ended 30 June 2008 the revaluation of this derivative caused Telecom to recognise a gain of NZ$4 million in the income statement (30 June 2007: loss of NZ$2 million).

Parent Company

The Parent Company's financial instruments were classified under NZ IFRS as follows:

PARENT AS AT 30 JUNE 2008 (DOLLARS IN MILLIONS)		AVAILABLE -FOR-SALE NZ$M	LOANS AND RECEIVABLES NZ$M	AMORTISED COST NZ$M	TOTAL CARRYING AMOUNT NZ$M
Current assets:	Receivables due from subsidiaries	-	689	-	689
Non-current assets:	Long-term investments	6,256	3,006	-	9,262
Current liabilities:	Debt due within one year	-	-	(5,764)	(5,764)
Non-current liabilities:	Long-term debt	-	-	(2,846)	(2,846)

PARENT AS AT 30 JUNE 2007 (DOLLARS IN MILLIONS)		AVAILABLE -FOR-SALE NZ$M	LOANS AND RECEIVABLES NZ$M	AMORTISED COST NZ$M	TOTAL CARRYING AMOUNT NZ$M
Current assets:	Receivables due from subsidiaries	-	795	-	795
Non-current assets:	Long-term investments	6,585	3,006	-	9,591
Current liabilities:	Debt due within one year	-	-	(4,993)	(4,993)
Non-current liabilities:	Long-term debt	-	-	(2,442)	(2,442)

The Parent Company has no derivative financial instruments.

Currency risk

Long-term debt amounts are denominated in Australian dollars. The Parent does not take any action to reduce its exposure to any resulting currency risk as long-term debt relates to amounts owed to wholly-owned subsidiaries.

Interest rate risk

The Parent Company has interest rate exposures on some loans to and from subsidiary companies. The Company does not manage the associated risks.

The Parent Company's maximum exposure to liquidity risk relating to financial liabilities is summarised below:

Parent (DOLLARS IN MILLIONS)	CARRYING AMOUNT NZ$M	CONTRACTUAL CASH FLOWS NZ$M	0-6 MONTHS NZ$M	6-12 MONTHS NZ$M	1-2 YEARS NZ$M	2-3 YEARS NZ$M	3-4 YEARS NZ$M	4-5 YEARS NZ$M	5+ YEARS NZ$M
Debt due to subsidiaries:									
30 June 2008	(8,610)	(8,610)	(5,764)	-	-	-	-	-	(2,846)
30 June 2007	(7,435)	(7,435)	(4,993)	-	-	-	-	-	(2,442)

Credit risk

The Parent Company has exposure to credit risk from balances owed from subsidiary companies. The maximum exposure to credit risk at 30 June 2008 is NZ$3,695 million (30 June 2007 NZ$3,801 million).

Equity risk

The Parent Company has exposure to equity risk by way of its investments in subsidiaries. The maximum exposure at 30 June 2008 of NZ$6,256 million (30 June 2007 NZ$6,585 million).

Hedging activities

The Parent Company has no hedging activities.

Note 27 Commitments

Operating leases

Minimum rental commitments for all non-cancellable operating leases are:

30 JUNE (DOLLARS IN MILLIONS)	GROUP 2008 NZ$M	2007 NZ$M
Less than 1 year	73	52
Between 1 - 5 years	206	137
More than 5 years	214	58
	493	**247**

Minimum rental commitments for operating leases increased during the year ended 30 June 2008 due to Telecom entering into new leases for office accommodation. These leases do not commence until 2011.

Finance Leases

At 30 June 2008 Telecom had no remaining commitments in respect of capitalised finance leases.

Capital commitments

At 30 June 2008 capital expenditure amounting to NZ$259 million (30 June 2007: NZ$91 million) had been committed under contractual arrangements, with substantially all payments due within one year. The capital expenditure commitments principally relate to telecommunications network assets.

Note 28 Contingencies

Lawsuits and other claims

New Zealand

In March 2004 the Commerce Commission issued proceedings against Telecom claiming that its implementation and maintenance of new retail and wholesale high speed data transmission service pricing since 1998 constituted a breach by Telecom of section 36 of the Commerce Act (abuse of a dominant position/taking advantage of market power). The Commission seeks a declaration that section 36 of the Commerce Act was breached, a pecuniary penalty, and costs. The trial was completed in early August 2008. The court has reserved its decision.

In July 2000 the Commerce Commission issued a proceeding against Telecom claiming that the introduction of 0867 constituted a use by Telecom of its dominant position for proscribed purposes. The Commerce Commission sought a declaration that this contravened section 36 of the Commerce Act, a pecuniary penalty, and costs. There was a six week trial in the Auckland High Court, which concluded on 26 September 2007. In a judgement issued on 16 April 2008 the High Court dismissed the Commission's proceeding, holding that Telecom's introduction of 0867 did not breach section 36 of the Commerce Act. The Commission has appealed the judgement.

Sintel (in liquidation) has issued proceedings against Telecom, relating to Telecom's audio text business in the 1990s. The matter was settled, but the liquidators are seeking to overturn the settlement agreement with various claims against Telecom, including fraud. Sintel filed an amended statement of claim, increasing the value of the claim to NZ$60 million. Telecom's application to strike out all but one of the causes of action was unsuccessful. In a judgement dated 14 November 2007 the Court of Appeal dismissed Telecom's appeal. Telecom has decided not to appeal the judgement and is now proceeding towards trial of the substantive matter. Telecom has received notices requesting additional information and responses. A judicial settlement conference is scheduled for 10 October 2008.

Asia Pacific Telecommunications Limited (APT) has also issued proceedings against Telecom in relation to its audio text business. The total claim is for approximately US$17 million plus an unquantifiable inquiry into damages based on the discovery documents. Telecom believes it has a strong defence for the majority of the claim. These proceedings will be vigorously defended by Telecom. The parties are working towards mediation. A fixture was allocated for August 2008 but due to an increased discovery request by APT this date has been vacated. Telecom is engaging in settlement dialogue with APT and both parties have expressed a desire to settle prior to any court fixture.

The Commerce Commission has laid charges against Telecom for alleged breaches of the Fair Trading Act in relation to a retail broadband advertising campaign that was run from October 2006. The allegation is that Telecom engaged in conduct that was liable to mislead the public as to the characteristics of services and made false or misleading representations about the performance characteristics of the retail plan at issue. Telecom is working through the details of the specific charges. However, at this stage it cannot quantify the potential impact of penalties or customer refunds should a court ultimately find in favour of the Commission.

In April 2007, Vodafone appealed the Commerce Commission's 2003/2004 TSO Determination. The appeal was dismissed in the High Court in December 2007, however Vodafone is seeking leave to appeal to the Court of Appeals. Telecom has opposed Vodafone's application for leave and its substantive appeal. The Court of Appeal has allocated a fixture in February 2009.

Telecom has been joined as one of numerous respondents in a claim lodged through the Weathertight Homes Resolution Services ('WHRS'). The claim relates to a property development site called 'Ellerslie Park' where Telecom installed external telephone junction boxes . While the claim against Telecom is small, liability could be joint and several. Telecom has applied to strike out the claim.

Previous arbitration proceedings by a former mobile phone salesman, Mr Holmes, were struck out by the High Court, however, Holmes has appealed this with the Court of Appeal.

Telecom has other ongoing Commerce Commission claims and investigations, none of which are expected to have significant effect on the financial position or profitability of Telecom.

All of the proceedings summarised above have been commenced in the High Court of New Zealand unless otherwise stated.

Australia

Telecom is in dispute with Pacific Union Group Pty Limited in respect of the withdrawal of certain product lines from the scope of the dealer agreement between the parties. Pacific Union has commenced proceedings in the Supreme Court of New South Wales, claiming breach of contract and/or repudiation of contract. The amount of loss and damage claimed has not yet been quantified by Pacific Union.

Telstra Corporation Limited has commenced proceedings in the Federal Court of Australia, and is seeking an order that the final determination made by the Australian Competition and Consumer Commission (ACCC) in a line sharing service arbitration be set aside on administrative law grounds. Telecom, amongst others, is a defendant in these proceedings. The Court has heard the case and Telecom awaits judgement.

Telstra Corporation Limited commenced proceedings in April 2008 in the Federal Court of Australia seeking an order that the final determination made by the ACCC in an unbundled local loop service arbitration be set aside on administrative law grounds. The hearing is scheduled for September 2008.

Various other lawsuits, claims and investigations have been brought or are pending against Telecom and its subsidiaries, none of which are expected to have significant effect on the financial position or profitability of Telecom.

The directors of Telecom do not believe an adverse outcome is probable and therefore cannot reasonably estimate the financial effect (if any) on Telecom if any of the foregoing claims are ultimately resolved against Telecom's interests. There can be no assurance that such litigation will not have a material adverse effect on Telecom's business, financial condition or results of operations.

Land claims

As previously stated in note 16, interests in land included in property, plant and equipment purchased from the Government may be subject to claims to the Waitangi Tribunal or deemed to be wāhi tapu and, in either case, may be resumed by the Government. Certain claims have been brought or are pending against the Government under the Treaty of Waitangi Act 1975. Some of these claims may affect land transferred to the Company by the Government and/or by the Company to its subsidiary companies. In the event that land is resumed by the Government, there is provision for compensation to Telecom.

Bank guarantees

Telecom has issued bank guarantees totalling A$4 million as at 30 June 2008 (30 June 2007: A$5 million) to guarantee rental payments of a subsidiary company. In the event of the subsidiary defaulting on these rental payments then Telecom has guaranteed to pay these amounts. The likelihood of any payments being made under this guarantee is low.

Cross border lease guarantees

Telecom has entered into several cross border leases in respect of certain telecommunications assets. Telecom has given certain undertakings including letters of credit in accordance with limited guarantees entered into as part of the transactions. The likelihood of losses in respect of these matters is considered to be remote. The maximum exposure under these guarantees is NZ$277 million (30 June 2007: NZ$310 million) and the last guarantee expires in 2016.

Parent company

The Parent Company has guaranteed, along with guaranteeing subsidiary companies, indebtedness of TCNZ Finance Limited (a Telecom group company) amounting to NZ$2,429 million (30 June 2007: NZ$2,469 million) under guarantees dated 21 August 2001 and 13 April 2006, and trust deeds dated 25 October 1988 and 17 March 2000 together with subsequent supplemental trust deeds and interest thereon. The Parent Company has issued further guarantees in relation to commercial paper and other treasury activities of TCNZ Finance Limited.

Note 29 Related party transactions

Interest of directors in certain transactions

Certain directors have relevant interests in a number of companies with which Telecom has transactions in the normal course of business. A number of Telecom's directors are also non-executive directors of other companies. Any transactions undertaken with these entities have been entered into on an arm's length commercial basis.

Advances to associate companies

During the year ended 30 June 2007 an advance to Southern Cross Cables Holdings Limited ('Southern Cross') of NZ$85 million was fully repaid.

Other transactions with associate companies

Telecom has the following transactions with Associates:

- Telecom provides network operations and management services to Southern Cross in respect of its operations in New Zealand. Telecom makes payments to Southern Cross in connection with capacity it has purchased on Southern Cross' network
- Telecom provides maintenance and telecommunications services to Yahoo!Xtra New Zealand Limited
- Telecom provides wholesale telecommunications services to Community Telco Australia Pty Limited.

Transactions undertaken with these entities have been entered into on an arm's length commercial basis. Balances in respect of these transactions with associate companies are set out in the table below.

	GROUP		
YEAR ENDED 30 JUNE	2008	2007	2006
(DOLLARS IN MILLIONS)	NZ$M	NZ$M	NZ$M
Revenue from associates[1]	125	54	40
Expenses paid to associates	6	7	7
Capacity acquired from associates[2]	16	30	-
Receivables from associates	8	4	6
Payables to associates	-	-	1

1 Includes dividends received from Southern Cross of NZ$89 million in 2008 (2007: NZ$18 million). No dividends were received in 2006.
2 Telecom's intangible assets includes capacity acquired from Southern Cross, with a cost of NZ$468 million (30 June 2007: NZ$449 million) and accumulated amortisation of NZ$178 million (30 June 2007: NZ$140 million).

Parent company

Amounts due from subsidiary companies are for no fixed term and are at interest rates that range from nil to 10%. Amounts due to subsidiary companies are for no fixed term and are at a weighted average interest rate of 8.12% at 30 June 2008 (30 June 2007: 7.87%).

Note 30 Subsidiary and associate companies

At 30 June 2008, the significant companies of the Telecom group and their activities were as follows:

	COUNTRY	OWNERSHIP	PRINCIPAL ACTIVITY
Subsidiary Companies			
TCNZ Australia Investments Pty Limited	Australia	100%	A holding company.
Telecom New Zealand International Australia Pty Limited	Australia	100%	Provides international wholesale telecommunications services.
TCNZ Australia Pty Limited	Australia	100%	Provides outsourced telecommunications services.
AAPT Limited	Australia	100%	Provides value-added telecommunications services.
PowerTel Limited	Australia	100%	Provides international wholesale telecommunications services.
Telecom New Zealand Finance (No.2) Limited	Bermuda	100%	A group finance company.
TCNZ (Bermuda) Limited	Bermuda	100%	A holding company.
Telecom Southern Cross Finance Limited	Bermuda	100%	A group finance company.
Telecom Cook Islands Limited	Cook Islands	60%	Provides telecommunications services in the Cook Islands.
Telecom Europe 3G ApS	Denmark	100%	A group finance company.
Telecom New Zealand Japan Kabushiki Kaisha	Japan	100%	Provides international wholesale telecommunications services.
Telecom New Zealand Limited	New Zealand	100%	Provides local, national, international and value-added telephone and data services.
Telecom Mobile Limited	New Zealand	100%	Provides mobile telecommunications services.
Xtra Limited	New Zealand	100%	Internet service provider.
Telecom Retail Holdings Limited	New Zealand	100%	Retailer of telecommunications products and services.
Telecom IP Limited	New Zealand	100%	Owns group intellectual property.
TCNZ Finance Limited	New Zealand	100%	A group finance company.
Telecom New Zealand Finance Limited	New Zealand	100%	A group finance company.
Telecom Southern Cross Limited	New Zealand	100%	A holding company.
Telecom New Zealand UK Limited	United Kingdom	100%	Provides international wholesale telecommunications services.
Telecom New Zealand USA Limited	United States	100%	Provides international wholesale telecommunications services.
Associate Companies			
Pacific Carriage Holdings Limited	Bermuda	50%	A holding company.
Southern Cross Cables Holdings Limited	Bermuda	50%	A holding company.
Community Telco Australia Pty Limited	Australia	50%	Community telecommunications franchise model.
Yahoo!Xtra Limited	New Zealand	49%	Internet services provider.

The financial year-end of all significant subsidiaries and associates is 30 June.

Note 31 Segmental reporting

Business segments

Results are reported for four operating segments, being the group's main areas of operations and a Corporate and Other amount containing revenues and costs not allocated to those operating segments. Telecom's segments consist of:

- NZ Business – Provider of calling, mobile, internet and data products to business customers in New Zealand
- NZ Consumer – Provider of calling, mobile, internet and data products to residential customers in New Zealand
- NZ Technology & Enterprises – Responsible for Telecom's network, IT and shared service capability throughout New Zealand and the delivery of services to wholesale customers
- Australian Operations – Provider of telecommunications services to residential and business customers in Australia

Corporate and Other includes those revenues and costs not associated with an operating segment, such as dividends from investments, head office support services for the group and international operations.

During the year ended 30 June 2007 Telecom sold Yellow Pages Group. The segmental reporting has been restated so that only continuing operations have been included. Segmental reporting for the discontinued operation is presented in note 36 and consists solely of Yellow Pages Group.

The segment result is measured on earnings before finance income and costs, associates losses and taxation expense. Where there are inter-segment sales they are priced on an arm's-length basis.

As at and for the year ended 30 June 2008

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS)	NZ BUSINESS NZ$M	NZ CONSUMER NZ$M	NZ TECHNOLOGY AND ENTERPRISES NZ$M	AUSTRALIAN OPERATIONS NZ$M	TOTAL OPERATING SEGMENTS NZ$M
Operating revenue:					
External customers	1,805	1,611	449	1,414	5,279
Internal customers	6	-	44	17	67
Total revenue	1,811	1,611	493	1,431	5,346
Segment result	977	1,024	(847)	(49)	1,105
Other information:					
Finance income	-	-	-	2	2
Finance expense	1	-	-	3	4
Depreciation and amortisation	19	22	519	144	704
Capital expenditure	81	19	723	112	935
Other gains	-	-	-	7	7
Balance sheet:					
Segment assets	230	1,286	3,554	1,075	6,145
Segment liabilities	81	374	490	217	1,162

As at and for the year ended 30 June 2007

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS)	NZ BUSINESS NZ$M	NZ CONSUMER NZ$M	NZ TECHNOLOGY AND ENTERPRISES NZ$M	AUSTRALIAN OPERATIONS NZ$M	TOTAL OPERATING SEGMENTS NZ$M
Operating revenue:					
External customers	1,799	1,709	414	1,310	5,232
Internal customers	3	-	29	17	49
Total revenue	1,802	1,709	443	1,327	5,281
Segment result	1,074	1,085	(811)	(51)	1,297
Other information:					
Finance income	-	-	6	-	6
Finance expense	1	-	-	1	2
Depreciation and amortisation	20	14	470	78	582
Capital expenditure	50	27	560	147	784
Other expenses	-	16	-	22	38
Balance sheet:					
Segment assets	157	1,370	3,337	816	5,680
Segment liabilities	71	337	462	252	1,122

As at and for the year ended 30 June 2006

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS)	NZ BUSINESS NZ$M	NZ CONSUMER NZ$M	NZ TECHNOLOGY AND ENTERPRISES NZ$M	AUSTRALIAN OPERATIONS NZ$M	TOTAL OPERATING SEGMENTS NZ$M
Operating revenue:					
External customers	1,822	1,689	399	1,305	5,215
Internal customers	1	-	21	18	40
Total revenue	1,823	1,689	420	1,323	5,255
Segment result	1,123	1,110	(792)	(1,386)	55
Other information:					
Finance expense	1	-	-	-	1
Depreciation and amortisation	16	11	434	169	630
Capital expenditure	48	15	529	131	723
Impairment	-	-	-	1,301	1,301
Other expenses	-	7	22	-	29
Balance sheet:					
Segment assets	106	1,359	3,258	529	5,252
Segment liabilities	78	282	225	164	749

Reconciliation from segmental external revenue to operating revenues and other gains

(DOLLARS IN MILLIONS)	2008 NZ$M	2007 NZ$M	2006 NZ$M
Segmental external revenue	5,279	5,232	5,215
Dividends	89	19	-
Other gains	7	20	60
Other unallocated revenue	298	311	280
Operating revenues and other gains	**5,673**	**5,582**	**5,555**

Reconciliation from segment result to net earnings/(loss) from continuing operations

(DOLLARS IN MILLIONS)	2008 NZ$M	2007 NZ$M	2006 NZ$M
Segment result	1,105	1,297	55
Corporate and other	25	(15)	10
	1,130	1,282	65
Finance income	119	59	28
Finance expense	(271)	(289)	(282)
Share of associates' net losses	(3)	(3)	-
Income tax expense	(262)	(205)	(351)
Net earnings/(loss) from continuing operations	**713**	**844**	**(540)**

Reconciliation from segmental assets to total assets

(DOLLARS IN MILLIONS)	2008 NZ$M	2007 NZ$M
Segmental assets	6,145	5,680
Corporate and other	1,260	2,596
Total assets	**7,405**	**8,276**

Reconciliation from segmental liabilities to total liabilities

(DOLLARS IN MILLIONS)	2008 NZ$M	2007 NZ$M
Segmental liabilities	1,162	1,122
Corporate and other	3,507	3,550
Total liabilities	4,669	4,672

Geographic segments

Disclosure of revenues, earnings before interest and taxation, property, plant and equipment, total assets and capital expenditure on a geographical basis is set out below. Each segment's total assets represents Telecom's external assets by segment and excludes inter-segment funding as interest is not allocated to segments. There are no other significant inter-segment intercompany assets or liabilities. Where recognised, inter-segment sales are priced on an arm's length basis.

GROUP AS AT AND FOR THE YEAR ENDED 30 JUNE 2008 (DOLLARS IN MILLIONS)	NEW ZEALAND NZ$M	AUSTRALIA NZ$M	OTHER NZ$M	ELIMINATIONS NZ$M	TOTAL NZ$M
Operating revenue					
External customers	4,100	1,414	152	-	**5,666**
Internal customers	71	17	8	(96)	**-**
Total revenue	4,171	1,431	160	(96)	**5,666**
Segment property, plant and equipment	3,379	574	31	-	**3,984**
Segment total assets	5,491	1,106	808	-	**7,405**
Capital expenditure	875	112	-	-	**987**

GROUP AS AT AND FOR THE YEAR ENDED 30 JUNE 2007 (DOLLARS IN MILLIONS)	NEW ZEALAND NZ$M	AUSTRALIA NZ$M	OTHER NZ$M	ELIMINATIONS NZ$M	TOTAL NZ$M
Operating revenue					
External customers	4,173	1,310	79	-	**5,562**
Internal customers	84	17	8	(109)	**-**
Total revenue	4,257	1,327	87	(109)	**5,562**
Segment property, plant and equipment	3,157	495	29	-	**3,681**
Segment total assets	5,197	843	2,236	-	**8,276**
Capital expenditure	689	143	-	-	**832**

GROUP AS AT AND FOR THE YEAR ENDED 30 JUNE 2006 (DOLLARS IN MILLIONS)	NEW ZEALAND NZ$M	AUSTRALIA NZ$M	OTHER NZ$M	ELIMINATIONS NZ$M	TOTAL NZ$M
Operating revenue					
External customers	4,140	1,289	66	-	**5,495**
Internal customers	3	2	9	(14)	**-**
Total revenue	4,143	1,291	75	(14)	**5,495**
Segment property, plant and equipment	3,079	182	40	-	**3,301**
Segment total assets	4,610	620	973	-	**6,203**
Capital expenditure	608	132	-	-	**740**

Note 32 Reconciliation of net earnings attributable to shareholders to net cash flows from operating activities

	GROUP			PARENT	
YEAR ENDED 30 JUNE	2008	2007	2006	2008	2007
(DOLLARS IN MILLIONS)	NZ$M	NZ$M	NZ$M	NZ$M	NZ$M
Net earnings/(loss) for the year	713	3,027	(431)	40	2,656
Adjustments to reconcile net earnings/(loss) to net cash flows from operating activities					
Depreciation and amortisation	761	658	705	-	-
Bad and doubtful accounts	34	40	38	-	-
Deferred income tax	83	(20)	82	-	-
Share of associates' losses	3	3	-	-	-
Gain on sale/purchase of subsidiaries and shares	-	(2,104)	(60)	-	-
Non-cash impairment	-	-	1,301	19	-
Other	(3)	58	25	404	637
Changes in assets and liabilities net of effects of non-cash and investing and financing activities					
Decrease/(increase) in accounts receivable and related items	43	(23)	44	83	-
Decrease/(increase) in inventories	14	(19)	3	-	-
Decrease in current taxation	68	119	135	(2)	(26)
(Decrease)/increase in accounts payable and related items	(31)	(88)	(35)	-	-
Net cash flows from operating activities	**1,685**	**1,651**	**1,807**	**544**	**3,267**

Note 33 Imputation credit account

Dividends paid by New Zealand resident companies may include imputation credits representing the taxation already paid by the Company on the profits distributed. New Zealand resident shareholders may claim a tax credit equal to the value of the imputation credit attached to dividends. Overseas shareholders in general are not entitled to claim the benefit of any imputation credit. Overseas shareholders may benefit from supplementary dividends.

The movements in the imputation credit accounts are detailed below:

	GROUP		
YEAR ENDED 30 JUNE	2008	2007	2006
(DOLLARS IN MILLIONS)	NZ$M	NZ$M	NZ$M
Credit at the beginning of the year	(190)	(297)	(518)
New Zealand income tax paid	(97)	(136)	(168)
Imputation credits attached to dividends paid	253	243	389
Credit at the end of the year	(34)	(190)	(297)

The Parent Company is a member of the Telecom Imputation Group. These imputation credits are available to attach to dividends paid by the Parent Company.

Note 34 Significant events after balance date

Declaration of dividend

On 7 August 2008 the board of directors approved the payment of a fourth quarter dividend of NZ$146 million, representing 8.0 cents per share. In addition, a supplementary dividend totalling approximately NZ$18 million will be payable to shareholders who are not resident in New Zealand. In accordance with the Income Tax Act 2007, Telecom will receive a tax credit from the Inland Revenue Department equivalent to the amount of supplementary dividends paid. The dividend payment dates will be 12 September 2008 for shares on the New Zealand and Australian Stock Exchanges and 19 September 2008 for shares on the New York Stock Exchange.

Debt issues

On 25 June 2008 Telecom launched a retail Telebond issue with maturities of 3 years, 5 years and 7 years. Interest rates are subject to change. As at 30 June 2008 interest rates being offered were 8.25%, 8.50% and 8.65% respectively. Telecom raised NZ$142 million under the Telebond issue which closed on 11 August 2008.

On 6 August 2008 Telecom issued a 4-year CHF200 million bond (NZ$258 million) under the US$2 billion Euro Medium Term Note Programme. The bond has an effective hedged fixed interest rate of 8.9%.

Note 35 Acquisition of subsidiaries

In February 2008 Telecom acquired Computer Plus Otago ('Computer Plus') for NZ$4 million in cash. Computer Plus is the Gen-i franchise operating in the Dunedin and Queenstown markets. This gave rise to NZ$4 million of goodwill.

In May 2007 Telecom acquired a 100% shareholding in PowerTel Limited (a wholesale telecommunications provider in Australia) for NZ$366 million (A$320 million of cash and A$6 million of associated costs). PowerTel incurred a net loss of NZ$1 million for the two-month period ended 30 June 2007.

The effect of this acquisition on the group's assets and liabilities on acquisition date was:

(DOLLARS IN MILLIONS)	PRE-ACQUISITION CARRYING AMOUNTS NZ$M	FAIR VALUE ADJUSTMENTS NZ$M	RECOGNISED VALUES ON ACQUISITION NZ$M
ASSETS			
Current assets:			
Cash	19	-	19
Receivables and prepayments	51	-	51
Goodwill	36	(36)	-
Investments	36	-	36
Total current assets	**142**	**(36)**	**106**
Deferred tax asset	12	(8)	4
Property, plant and equipment	132	181	313
Total assets	**286**	**137**	**423**
LIABILITIES			
Current liabilities:			
Interest bearing debt	(50)	-	(50)
Deferred tax liability	(4)	-	(4)
Other liabilities	(66)	-	(66)
Total liabilities	**(120)**	**-**	**(120)**
Net identifiable assets and liabilities			303
Goodwill arising on acquisition			63
Consideration paid			366
Less cash acquired			(19)
Net consideration paid			347

The goodwill arose due to the synergies that Telecom expects to realise through the integration of PowerTel into its Australian operations.

The following proforma summary presents the group as if the acquisitions had been made on 1 July 2006. The proforma amounts below are unaudited, do not include any possible synergies from the acquisition and are provided for comparative purposes only and do not necessarily reflect the actual results that would have occurred, nor is it necessarily indicative of future results of operations of the combined companies.

YEAR ENDED 30 JUNE (DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS)	GROUP (UNAUDITED) 2007 NZ$M
Revenue	5,755
Net earnings/(loss) attributable to shareholders	3,008
Basic earnings per share	NZ$1.51

Note 36 Discontinued operations

Telecom completed the sales process for Yellow Pages Group on 30 April 2007. The 2006 income statement has been re-presented to show the Yellow Pages Group results as a discontinued operation, separately from Telecom's continuing operations. The results for the Yellow Pages Group also represent the discontinued operation for segmental purposes. The results for the periods presented in the income statement are as follows:

	GROUP	
(DOLLARS IN MILLIONS, EXCEPT PER SHARE AMOUNTS)	2007 NZ$M	2006 NZ$M
Operating revenues	**232**	**260**
Operating expenses		
Labour	(33)	(36)
Other operating expenses	(53)	(66)
Depreciation	(2)	(2)
Amortisation	(4)	(4)
Net earnings before taxation	140	152
Income tax expense	(41)	(43)
Net earnings after taxation	99	109
Gain on sale of discontinued operation	2,084	-
Net earnings from discontinued operation	**2,183**	**109**
Basic earnings per share (in cents)	NZ$1.10	NZ$0.06
Diluted earnings per share (in cents)	NZ$1.08	NZ$0.06
Gain on sale of discontinued operation		
Cash	2,161	-
Less: net assets disposed of	(27)	-
Less: associated costs on sale	(50)	-
Gain on sale of discontinued operation	**2,084**	**-**

The cash flows of the Yellow Pages Group were as follows:

	GROUP	
(DOLLARS IN MILLIONS)	2007 NZ$M	2006 NZ$M
Cash flows from operating activities	123	94
Cash flows from investing activities	(24)	(18)
Net cash flow	**99**	**76**

The major classes of assets and liabilities of the Yellow Pages Group at the disposal date were as follows:

(DOLLARS IN MILLIONS)	30 APRIL 2007 NZ$M
Assets	
Receivables and prepayments	16
Intangible assets	21
Property, plant and equipment	21
Liabilities	
Accounts payable and accruals	(31)
Net assets of Yellow Pages Group at date of disposal	**27**

Note 37 New accounting standards

Certain new standards, amendments and interpretations to existing standards have been published that are mandatory for Telecom's accounting periods beginning on or after 1 July 2008, but which Telecom has not yet adopted. Telecom does not consider any other standards or interpretations in issue, but not yet applicable, to have a significant impact on its financial statements. Those which are relevant to Telecom are as follows:

IAS/NZ IAS 1 Presentation of financial statements (revised)

Effective for periods beginning on or after 1 January 2009

The revised standard introduces total comprehensive income (changes in equity during a period, other than those resulting from transactions with owners in their capacity as owners) and a statement of comprehensive income.

All non-owner changes in equity are presented in one statement or two statements. The revised standard also prohibits presenting components of comprehensive income in the statement of changes in equity. Telecom's disclosures will change upon adoption in the year ending 30 June 2010.

IAS/NZ IAS 23 Borrowing costs

Effective for periods beginning on or after 1 January 2009

The main change is the removal of the option to expense borrowing costs incurred in respect of 'qualifying assets' for full reporting entities. Telecom currently capitalises directly attributable borrowing costs.

IAS/NZ IAS 27 Consolidated and separate financial statements

Effective for periods beginning on or after 1 July 2009

The amendment requires the effects of all transactions with non controlling interests to be recorded in equity if there is no change in control. Such transactions will no longer result in goodwill or gains or losses being recorded. It also specifies that when control is lost, any remaining interest should be re-measured to fair value and a gain or loss recorded through the income statement. No impact is anticipated upon adoption in the year ending 30 June 2010.

IFRS/NZ IFRS 2 Amendments to share based payments

Effective for periods beginning on or after 1 July 2009

The amendment defines vesting conditions to clarify that vesting conditions are limited to service conditions and performance conditions. No impact is anticipated on the accounting for share based payments upon adoption in the year ending 30 June 2010.

IFRS/NZ IFRS 3 Business combinations (revised 2008)

Effective for periods beginning on or after 1 July 2009

Includes in its scope business combinations involving only mutual entities, and those in which separate entities or businesses are brought together to form a reporting entity by contract alone. In addition to this are new or amended requirements such that all items of consideration transferred are recognised at fair value, transaction and acquisition costs must be expensed as incurred, additional acquisition of non-controlling equity interests after the business combination accounted for as an equity transaction and new disclosures. The standard must be applied prospectively and will impact the accounting for any future business combinations made after upon adoption for the year ending 30 June 2010.

IFRS/NZ IFRS 4 Insurance contracts – amendments

Effective for periods beginning on or after 1 January 2009

The amendment removes the partial exemption for qualifying entities, now requiring full compliance for qualifying entities. No impact is anticipated from adoption of the amendment upon adoption in the year ending 30 June 2010.

IFRS/NZ IFRS 8 Operating segments

Effective for periods beginning on or after 1 January 2009

The new standard introduces a management reporting approach to identifying and measuring the results of reportable operating segments. Telecom originally intended to adopt for the year ended 30 June 2008. However, Telecom now intends to adopt this standard from 1 July 2008 to align adoption with its reporting under its new organisational structure. The combination of the new business units and the application of the standard will change the presentation of Telecom's segmental information.

IFRIC/NZ IFRIC 13 Customer loyalty programmes

Effective for periods beginning on or after 1 July 2008

This interpretation addresses how companies that grant their customers loyalty award credits (sometimes referred to as 'points') when buying goods or services, should account for their obligation to provide free or discounted goods or services, if and when the customer redeems the points. The interpretation is effective for annual periods beginning on or after 1 July 2008, with early application permitted. The group intends to adopt this interpretation for the year ending 30 June 2009 and is evaluating the impact of adoption.