TELECO INSURANCE (NZ) LIMITED

FINANCIAL STATEMENTS

For the year ended 30 June 2012

This annual report is signed on behalf of the Board by:

Richard Quince
DIRECTOR

Mark Laing
DIRECTOR

DATE 19 October 2012

COMPANY DIRECTORY

Nature of business:	Insurance
Registered Office:	Level 2 Telecom Place 167 Victoria Street West, AUCKLAND, 1142
Company registration number	509425
Directors	Richard Quince, Mark Leslie Laing,
Shareholder	Telecom Corporation of New Zealand Limited
Auditors	KPMG 10 Customhouse Quay Wellington
Bankers	Westpac Banking Corporation

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 30 JUNE 2012

	Notes	30 June 2012	30 June 2011
		$000's	$000's
Insurance premiums		4,040	3,206
Expenses			
Claims incurred	2	(2,359)	(2,667)
Operating expenses	3	(88)	(178)
Underwriting surplus		**1,593**	**361**
Investment income	4	1,869	2,417
Profit before income tax		**3,462**	**2,778**
Income tax	5	(984)	(834)
Total Comprehensive Income for the period		**2,478**	**1,944**

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 30 JUNE 2012	Share Capital	Retained Earnings	Total Equity
	$000's	$000's	$000's
Balance at 1 July 2010	1	30,799	30,800
Profit for the year	-	1,944	1,944
Total comprehensive income for the period	-	1,944	1,944
Dividends	-	(8,400)	(8,400)
Balance at 30 June 2011	**1**	**24,343**	**24,344**
Balance at 1 July 2011	1	24,343	24,344
Profit for the year	-	2,478	2,478
Total comprehensive income for the period	-	2,478	2,478
Balance at 30 June 2012	**1**	**26,821**	**26,822**

The accompanying notes form part of and are to be read in conjunction with these financial statements.

BALANCE SHEET

AS AT 30 JUNE 2012

	Notes	30 June 2012	30 June 2011
		$000's	$000's
ASSETS			
Current assets:			
Interest receivable		44	4
Amounts owing from related parties	10	33,682	30,976
Total current assets		**33,726**	**30,980**
Non current asset:			
Investments – government securities		500	500
Total assets		**34,226**	**31,480**
LIABILITIES AND EQUITY			
Current liabilities:			
Accounts payable		-	122
Tax payable	5	984	1,018
Amounts owing to related parties	10	249	207
Fire Service levies payable		50	50
Unearned revenue		227	-
Outstanding claims liability	6	394	239
Total current liabilities		**1,904**	**1,636**
Non-current liabilities:			
Redeemable preference shares	7	**5,500**	**5,500**
Total liabilities		**7,404**	**7,136**
Equity:			
Retained earnings	8	26,821	24,343
Share capital		1	1
Total equity		**26,822**	**24,344**
Total liabilities and equity		**34,226**	**31,480**

The accompanying notes form part of and are to be read in conjunction with these financial statements.

Approved by the directors

Richard Quince
DIRECTOR

Mark Leslie Laing
DIRECTOR

Authorised for issue on 19 October 2012

NOTES TO THE FINANCIAL STATEMENTS

Note 1 ACCOUNTING POLICIES

OWNERSHIP AND ACTIVITIES

Teleco Insurance (NZ) Limited (the "Company") was incorporated in New Zealand on 18 July 1991 in the name of Telecom North Limited as a wholly-owned subsidiary of Telecom Corporation of New Zealand Limited (the "parent company" or "Telecom"). The Company changed its name to Teleco Insurance (NZ) Limited effective from 1 August 1995. Telecom and its subsidiaries together form the "Telecom Group".

The principal activity of the Company is to provide insurance policies for mobile phone handsets sold by the Telecom Retail Business unit. The Company has a credit rating with Standards and Poor's of BBB+, which was reaffirmed on 7 February 2012.

BASIS OF PREPARATION

The Company is a profit-orientated entity. The Company is a reporting entity for the purposes of the Financial Reporting Act 1993 and its financial statements comply with that Act.

These financial statements have been prepared in accordance with New Zealand Generally Accepted Accounting Practice ("NZ GAAP"). They comply with the New Zealand equivalents to New Zealand International Financial Reporting Standards ("NZ IFRS") and other applicable Financial Reporting Standards as appropriate for profit-orientated entities that qualify for and apply Differential Reporting concessions.

DIFFERENTIAL REPORTING

In accordance with the Framework for Differential Reporting under NZ IFR issued by the Institute of Chartered Accountants of New Zealand, the Company qualifies for the Differential Reporting exemptions as it has no public accountability, and the Company's owner is represented on the governing body. The Company has taken advantage of Differential Reporting exemptions available to it.

The accounting policies set out in the Statements of Accounting Policies have been applied in preparing financial statements for the year ended 30 June 2012 and for the comparative information presented for the year ended 30 June 2011.

PRESENTATION CURRENCY

The financial statements are presented in New Zealand dollars, the Company's functional currency.

MEASUREMENT BASIS

The measurement basis adopted in the preparation of these financial statements is historical cost, with the exception of surplus funds (or cash) invested with TCNZ Finance Limited ("TCNZ Finance") and outstanding claims liability which is based on the current retail price of mobile phones at date of claim. Both of these are stated at fair value.

PREMIUM REVENUE

Premium revenue comprises amounts charged to the policyholders. The earned portion of premiums received and receivable is recognised as revenue. Premium is earned over the indemnity period based on the pattern of risks underwritten, from the date of attachment of risk.

NOTES TO THE FINANCIAL STATEMENTS *(CONTINUED)*

FOREIGN CURRENCIES

Foreign currency transactions are translated to New Zealand dollars at the exchange rate ruling at the date of the transactions.

NON-DERIVATIVE FINANCIAL INSTRUMENT

Government Securities held to maturity pursuant to the Insurance Companies' Deposits Act 1953 are non-derivative financial assets that are measured at amortised cost using the effective interest method.

TAXATION

Taxation is accounted for using the taxes payable method, where income tax expense in the current period is the estimated income tax payable in the current period, adjusted for any differences between the estimated and actual income tax payable in prior periods. No deferred tax is recognised.

CLAIMS AND OUTSTANDING CLAIMS LIABILITY

Claims incurred expense consists of payment for claims and the movement in the outstanding claims liability. The claims liability includes a central estimate of claims reported but not yet paid; claims incurred but not yet reported; expected direct and indirect claims settlement costs, plus a risk margin.

The value of outstanding claims has not been discounted because the period between the date of claim and the settlement date is short (within one year) and the valuation estimates of an expected level of payment allows for current inflation.

Based on existing knowledge it is reasonably probable that outcomes within the next financial year may be different from the above assumptions and could result in a material adjustment to the carrying value of the claims provision.

CHANGES IN ACCOUNTING POLICIES

The accounting policies have been applied consistently to all periods presented in these financial statements.

Note 2 CLAIMS INCURRED	30 June 2012 $000's	30 June 2011 $000's
Claims incurred in current year	(1,898)	(2,013)
Reassessment of prior period claims	-	-
Risk margin adopted	(51)	-
Claims management fee	(410)	(735)
Total claims incurred expense	**(2,359)**	**(2,748)**

Note 3 OPERATING EXPENSES	30 June 2012 $000's	30 June 2011 $000's
Credit rating fee	(53)	(47)
Other administrative expenses	(35)	(131)
Total operating expenses	**(88)**	**(178)**

Audit fees for the year ended 30 June 2012 of $7,000 (2011: $7,500) were paid on the Company's behalf by a fellow subsidiary of the parent company. These are not recharged to the Company. Directors' fees paid for the year ended 30 June 2012 were nil (2011: nil).

Note 4 INVESTMENT INCOME	30 June 2012	30 June 2011
	$000's	$000's
Government securities – interest income	24	31
Intercompany interest income (refer note 9)	1,845	2,386
Total investment income	**1,869**	**2,417**

Note 5 INCOME TAX	30 June 2012	30 June 2011
	$000's	$000's
Profit before income tax	3,461	2,778
Income tax expense (at current rate of 28%: 2011: 30%)	969	834
Adjustment for non-deductible item	15	-
Total income tax expense	984	834
Opening balance of tax liability	1,018	582
Tax paid and inter-group allocation	(1,018)	(398)
Closing balance of tax payable	**984**	**1,018**

Note 6 OUTSTANDING CLAIMS LIABILITY	30 June 2012	30 June 2011
	$000's	$000's
Outstanding claims liability	343	239
Risk margin (15%)	51	-
Total current outstanding claims liability	**394**	**239**

The variation in outcome of the claims liability will be small because the valuation of claims for replacement mobile handsets is based on current retail prices, the number of open claims relating to the financial year is known, and the insurance settlement date is short.

Actuary, Paul Rhodes FNZSA FIA, has nominated a 15% risk margin based on industry benchmarking as reasonable to allow for uncertainty in the central estimate of claims and to achieve a 75% probability of sufficiency of the provision.

Reconciliation of Movement in Claims Liability:	30 June 2012	30 June 2011
	$000's	$000's
Balance at beginning of year	239	717
Injury claims provision transferred to Telecom New Zealand Limited	-	(393)
Claims notified	1,857	2,051
Claims paid	(1,793)	(2,098)
Adoption of a risk margin	51	-
Movement in claims incurred but not reported (IBNR)	40	(38)
Balance at end of year	**394**	**239**

Note 7 REDEEMABLE PREFERENCE SHARES

The Company has 550 fully paid redeemable preference shares on issue (2011: 550), each with a value of $10,000. The shares have no fixed repayment date and the holder, Telecom Corporation of New Zealand Limited, can ask for repayment at any time by providing written notice to the Company. The holder has no intention of requesting repayment within the next year.

Redeemable preference shares have no voting rights. The holder of the preference shares has the right on winding up of the Company to payment in priority to the holders of ordinary shares of the Company of the redemption amounts of each preference share held, calculated as at the date of distribution. All other rights conferred to the holder of either ordinary or preference shares are the same.

Note 8 EQUITY

As at 30 June 2012 there were 100 fully paid $1 ordinary shares on issue (2011:100). Each share confers on the holder the right to vote at any meeting of shareholders.

The Company maintains equity in the form of retained earnings of $26,822,000 (2011: $24,344,000), and the Directors believe that this is an appropriate level to cover its exposure to risk based on annual aggregate exposure and loss history.

Note 9 RISK MANAGEMENT

The Company is exposed to a number of risks in the normal course of business, primarily insurance risk, financial risk (liquidity risk and interest rate risk), and credit risk.

a. Insurance risk

The Company's main insurance risk is from the increasing value of smart phones which will impact on claim costs in the future. Therefore, the main risk management objective is to manage the magnitude and the volatility of claim costs. Aon New Zealand Limited, the claims administrator, also actively manages claim activity, with assistance from the Telecom Fraud team. The Company will review the premium rates by having the appointed actuary regularly review the premium rates to ensure that prices reflect risk.

For the Company a broader risk is the reliance on one line of business in a niche market (namely mobile handset insurance for post paid customers). If something were to arise that negatively affects this niche, such as reduced use of mobile phones, it would have a flow on impact on The Company's financial position. This is the same risk that the parent company has and the Company accepts this risk.

The probability of catastrophe risk causing a large number of handset replacement claims is low as the value of policies is relatively low and policyholders are geographically widespread throughout New Zealand.

b. Financial risk

Liquidity risk:

The risk of being unable to pay claims and operating expenses in a timely manner is negated by the Company holding surplus funds of $32,802,508 (2011: $29,169,321) in an on-call current account with TCNZ Finance Limited.

The Company has entered into an agreement with Westpac Banking Corporation to guarantee $18m of the $32.8m funds held by TCNZ Finance Limited, in order to mitigate the risk of asset concentration of these funds being held by a related party.

Interest risk:
There is minimal interest rate risk as surplus funds invested with TCNZ Finance Limited earn a fixed interest rate (6%). An interest risk exists when Government securities mature and a new security is purchased. These Government securities are held by the Public Trust of behalf on the Company pursuant to the Insurance Companies' Deposits Act 1953; (repealed on 7 March 2012) and to be held until full licence issued by September 2013.

c. Credit risk
The Company incurs credit risk related to financial assets of $34,226,000 (2011: $31,480,000).

Except for $500,000 invested in Government securities, the Company's funds are invested by TCNZ Finance Limited. The board of directors of TCNZ Finance Limited have approved a credit risk policy that limits exposure with counterparties by placing its cash and short-term investments with high credit quality financial institutions and sovereign bodies, and it also limits the amount of credit exposure to any one of these financial institutions.

Telecom (which guarantees TCNZ Finance's debt) has credit ratings from Standard & Poor's and Moody's Investors Services on its indebtedness. Details of current ratings at 30 June 2012 are as follows:

Standard & Poors		Moody's Investors Services	
Long Term Senior Debt	A-	Long Term Senior Debt	A3
Short Term Debt	A-2	Short Term Debt	P-2
Outlook	Stable	Outlook	Stable

Note 10 RELATED PARTIES

The Company's ultimate parent company is Telecom Corporation of New Zealand Limited. The Company has transactions with fellow subsidiaries as set out below:

Balances at 30 June	Amount owing by: 2012 $000's	2011 $000's	Amount owing to: 2012 $000's	2011 $000's
TCNZ Finance Limited	32,803	29,169	-	-
Telecom New Zealand Limited	879	1,807	(249)	(207)
Total of Related Party Balances at 30 June	**33,682**	**30,976**	**(249)**	**(207)**

Transactions occurring during the year:	2012 $000's	2011 $000's
TCNZ Finance Limited:		
Dividend payment	-	(8,400)
Net operating cash transactions	1,789	(4,380)
Interest received	1,845	2,386
Telecom New Zealand Limited:		
Replacement mobile handsets	(1,973)	(2,098)

Surplus funds are invested with TCNZ Finance. Funds are held on-call and earn fixed interest at 6% (2011: 6%).

NOTES TO THE FINANCIAL STATEMENTS *(CONTINUED)*

Note 10 RELATED PARTIES (continued)

At 30 June 2012, the Company owes amounts to Telecom for the reimbursement of expenses paid to suppliers and for replacement mobile handset provided to insurance claimants on the Company's behalf. No related party debts have been written off or forgiven during the year.

Note 11 CONTINGENT LIABILITIES

The Directors are not aware of any significant contingent liabilities at 30 June 2012 (30 June 2011: nil).

Note 12 CAPITAL COMMITMENTS

There are no capital commitments at 30 June 2012 (30 June 2011: nil).

Note 13 SUBSEQUENT EVENTS

There have been no events subsequent to balance date that impact these financial statements.

Independent auditor's report

To the shareholder of Teleco Insurance (NZ) Limited

Report on the financial statements

We have audited the accompanying financial statements of Teleco Insurance (NZ) Limited ("the company") on pages 1 to 8. The financial statements comprise the statement of financial position as at 30 June 2012, the statements of comprehensive income and changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory information.

Directors' responsibility for the financial statements

The directors is responsible for the preparation of financial statements in accordance with generally accepted accounting practice in New Zealand that give a true and fair view of the matters to which they relate, and for such internal control as the directors determines is necessary to enable the preparation of financial statements that are free from material misstatement whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing (New Zealand). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company's preparation of the financial statements that give a true and fair view of the matters to which they relate in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, as well as evaluating the presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Partners and employees of our firm may deal with the company on normal terms within the ordinary course of trading activities of the business of the. These matters have not impaired our independence as auditor of the company. The firm has no other relationship with, or interest in, the company.

Opinion

In our opinion the financial statements on pages 1 to 8:

- comply with generally accepted accounting practice in New Zealand;
- give a true and fair view of the financial position of the company as at 30 June 2012 and of its financial performance for the year then ended.

Report on other legal and regulatory requirements

In accordance with the requirements of sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993, we report that:

- we have obtained all the information and explanations that we have required; and
- in our opinion, proper accounting records have been kept by Teleco Insurance (NZ) Limited as far as appears from our examination of those records.

KPMG

19 October 2012
Wellington

The Board of Directors
Teleco Insurance (NZ) Limited
42-52 Willis Street
Wellington

7 December 2012

Appointed actuary's review of actuarial information for Teleco Insurance (NZ) Limited

To the Directors of Teleco Insurance (NZ) Limited,

This letter has been prepared for Teleco Insurance (NZ) Limited ("Teleco") to meet the requirements of Section 78 of the Insurance (Prudential Supervision) Act 2010 ("the Act") in respect of Section 77 of the Act which requires that each Licensed insurer must ensure that the actuarial information contained in, or used in preparation of, the financial statements of the insurer is reviewed by the appointed actuary.

I have reviewed the following actuarial information included in the audited accounts for Teleco as at 30 June 2012:

- Outstanding claims liability.

I have been provided with all the information and explanations that I have required to complete my review.

I am the appointed actuary to Teleco and am a Partner of PricewaterhouseCoopers New Zealand. I am independent of Teleco.

In my opinion:

- the actuarial information contained in the financial statements has been appropriately included in those statements; and
- the actuarial information used in the preparation of the financial statements has been used appropriately; and
- Teleco is maintaining a solvency margin as required under the Solvency Standard for Non-Life Insurance Business issued by the Reserve Bank of New Zealand.

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pwc

Reliances and limitations

This letter has been prepared for Teleco and is provided in accordance with the terms set out in our statement of work dated 17 September 2012.

No distribution of this letter to third parties, other than as required by law is permitted by us. There may be requests for our report to be copied to third parties. We will be happy to consider these requests, as and when they arise.

Our responsibilities and liabilities are limited to Teleco and exist only in the context of their use of our letter. No liability or responsibility will be accepted by us in relation to the use of our report for any other purpose. We will not accept any liability or responsibility to any third party recipients.

We have relied on information provided to us in the course of carrying out our work. We perform some data validation checks but we have not verified all of the information provided to us, nor have we carried out anything in the nature of an audit. Accordingly, we express no opinion on the total reliability, accuracy or completeness of the information provided to us and upon which we have relied. We have no reason to believe that the information provided to us is inaccurate or misleading.

This letter must be read in its entirety. Individual sections of this report could be misleading if considered in isolation from each other. If distributed, this letter must be distributed in its entirety.

This letter is not considered an actuarial report under Professional Standard 9.1 of the New Zealand Society of Actuaries.

Yours sincerely

Paul Rhodes, FNZSA, FIA