

PRIMUS TELECOMMUNICATIONS GROUP INC  
Form 10-Q  
August 11, 2008  
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# SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

## FORM 10-Q

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

For the quarterly period ended June 30, 2008

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934.

Commission File No. 0-29092

## PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

54-1708481  
(I.R.S. Employer Identification No.)

7901 Jones Branch Drive, Suite 900,

22102

McLean, VA  
(Address of principal executive offices)

(Zip Code)

(703) 902-2800

(Registrant's telephone number, including area code)

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

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes  No

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

| Class                         | Outstanding as of            |
|-------------------------------|------------------------------|
| Common Stock \$0.01 par value | July 31, 2008<br>142,632,540 |

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**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**  
**CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS**

(in thousands, except per share amounts)

(unaudited)

|  | Three Months Ended<br>June 30, |            | Six Months Ended<br>June 30, |            |
|--|--------------------------------|------------|------------------------------|------------|
|  | 2008                           | 2007       | 2008                         | 2007       |
| NET REVENUE  | \$ 236,462                     | \$ 226,430 | \$ 462,542                   | \$ 452,433 |
| OPERATING EXPENSES   |                                |            |                              |            |
| Cost of revenue (exclusive of depreciation included below)   | 142,739                        | 141,643    | 284,518                      | 285,659    |
| Selling, general and administrative                          | 70,247                         | 68,516     | 139,416                      | 136,212    |
| Depreciation and amortization                                | 8,095                          | 7,343      | 16,056                       | 13,900     |
| (Gain) loss on sale or disposal of assets                    | 115                            | 676        | (2,465)                      | 684        |
| Total operating expenses                                     | 221,196                        | 218,178    | 437,525                      | 436,455    |
| INCOME FROM OPERATIONS                                       | 15,266                         | 8,252      | 25,017                       | 15,978     |
| INTEREST EXPENSE   | (13,554)                       | (16,424)   | (28,747)                     | (29,858)   |
| ACCRETION ON DEBT PREMIUM (DISCOUNT), NET                    | 217                            | (76)       | 187                          | (374)      |
| GAIN (LOSS) ON EARLY EXTINGUISHMENT OR RESTRUCTURING OF DEBT | 32,177                         | (2,315)    | 34,487                       | (8,274)    |
| INTEREST AND OTHER INCOME                                    | 1,992                          | 1,058      | 2,957                        | 2,554      |
| FOREIGN CURRENCY TRANSACTION GAIN                            | 8,134                          | 15,081     | 9,841                        | 18,055     |
| INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES | 44,232                         | 5,576      | 43,742                       | (1,919)    |
| INCOME TAX BENEFIT (EXPENSE)                                 | 2,383                          | 6,691      | (37)                         | 5,686      |
| INCOME FROM CONTINUING OPERATIONS                            | 46,615                         | 12,267     | 43,705                       | 3,767      |
| LOSS FROM DISCONTINUED OPERATIONS, net of tax                | (91)                           | (166)      | (180)                        | (266)      |
| GAIN FROM SALE OF DISCONTINUED OPERATIONS, net of tax        |                                |            |                              | 5,958      |
| NET INCOME   | \$ 46,524                      | \$ 12,101  | \$ 43,525                    | \$ 9,459   |
| BASIC INCOME (LOSS) PER COMMON SHARE:                        |                                |            |                              |            |
| Income from continuing operations                            | \$ 0.33                        | \$ 0.11    | \$ 0.31                      | \$ 0.03    |
| Loss from discontinued operations                            | (0.00)                         | (0.01)     | (0.00)                       | (0.00)     |
| Gain from sale of discontinued operations                    |                                |            |                              | 0.05       |
| Net income   | \$ 0.33                        | \$ 0.10    | \$ 0.31                      | \$ 0.08    |
| DILUTED INCOME (LOSS) PER COMMON SHARE:                      |                                |            |                              |            |
| Income from continuing operations                            | \$ 0.25                        | \$ 0.07    | \$ 0.23                      | \$ 0.02    |
| Loss from discontinued operations                            | (0.00)                         | (0.00)     | (0.00)                       | (0.00)     |
| Gain from sale of discontinued operations                    |                                |            |                              | 0.04       |
| Net income   | \$ 0.25                        | \$ 0.07    | \$ 0.23                      | \$ 0.06    |
| BASIC WEIGHTED AVERAGE COMMON SHARES OUTSTANDING             | 142,633                        | 115,715    | 142,633                      | 114,928    |

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|  |         |         |         |         |
|--|---------|---------|---------|---------|
| DILUTED WEIGHTED AVERAGE COMMON SHARES OUTSTANDING | 190,328 | 184,719 | 195,221 | 184,467 |
|--|---------|---------|---------|---------|

See notes to consolidated financial statements.

**Table of Contents****PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED****CONSOLIDATED BALANCE SHEETS**

(in thousands, except share amounts)

(unaudited)

|  | June 30,<br>2008  | December 31,<br>2007 |
|--|-------------------|----------------------|
| <b>ASSETS</b>  |                   |                      |
| CURRENT ASSETS:  |                   |                      |
| Cash and cash equivalents  | \$ 55,550         | \$ 81,282            |
| Restricted cash  |                   | 362                  |
| Accounts receivable (net of allowance for doubtful accounts receivable of \$13,489 and \$12,039)   | 118,412           | 113,588              |
| Prepaid expenses and other current assets  | 19,470            | 28,660               |
| Total current assets   | 193,432           | 223,892              |
| RESTRICTED CASH  | 10,782            | 9,677                |
| PROPERTY AND EQUIPMENT Net   | 147,753           | 144,599              |
| GOODWILL   | 40,539            | 40,134               |
| OTHER INTANGIBLE ASSETS Net  | 989               | 1,557                |
| OTHER ASSETS   | 33,431            | 40,544               |
| <b>TOTAL ASSETS</b>  | <b>\$ 426,926</b> | <b>\$ 460,403</b>    |
| <b>LIABILITIES AND STOCKHOLDERS DEFICIT</b>  |                   |                      |
| CURRENT LIABILITIES:   |                   |                      |
| Accounts payable   | \$ 60,334         | \$ 74,893            |
| Accrued interconnection costs  | 49,396            | 44,911               |
| Deferred revenue   | 15,839            | 16,513               |
| Accrued expenses and other current liabilities   | 53,518            | 54,420               |
| Accrued income taxes   | 26,322            | 30,791               |
| Accrued interest   | 11,191            | 12,460               |
| Current portion of long-term obligations   | 9,301             | 11,228               |
| Total current liabilities  | 225,901           | 245,216              |
| LONG-TERM OBLIGATIONS (net of premium of \$4,452 and \$2,528)  | 608,876           | 662,675              |
| OTHER LIABILITIES  | 80                | 52                   |
| Total liabilities  | 834,857           | 907,943              |
| COMMITMENTS AND CONTINGENCIES (See Note 5.)  |                   |                      |
| STOCKHOLDERS DEFICIT:  |                   |                      |
| Preferred stock: Not Designated, \$0.01 par value 1,410,050 shares authorized; none issued and outstanding; Series A and B, \$0.01 par value 485,000 shares authorized; none issued and outstanding; Series C, \$0.01 par value 559,950 shares authorized; none issued and outstanding |                   |                      |
| Common stock, \$0.01 par value 300,000,000 shares authorized; 142,632,540 shares issued and outstanding  | 1,426             | 1,426                |
| Additional paid-in capital   | 718,827           | 718,695              |
| Accumulated deficit  | (1,031,253)       | (1,074,778)          |
| Accumulated other comprehensive loss   | (96,931)          | (92,883)             |

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|  |                   |                   |
|--|-------------------|-------------------|
| Total stockholders' deficit                        | (407,931)         | (447,540)         |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT</b> | <b>\$ 426,926</b> | <b>\$ 460,403</b> |

See notes to consolidated financial statements.

**Table of Contents****PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED****CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS**

(in thousands)

(unaudited)

|   | <b>Six Months Ended<br/>June 30,</b> |                 |
|---|--------------------------------------|-----------------|
|   | <b>2008</b>                          | <b>2007</b>     |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  |                                      |                 |
| Net income  | \$ 43,525                            | \$ 9,459        |
| Adjustments to reconcile net income to net cash provided by operating activities:                               |                                      |                 |
| Provision for doubtful accounts receivable  | 5,696                                | 4,885           |
| Stock compensation expense  | 132                                  | 125             |
| Depreciation and amortization   | 16,056                               | 13,946          |
| Gain on sale or disposal of assets  | (2,465)                              | (5,078)         |
| Accretion of debt discount (premium)  | (187)                                | 374             |
| Deferred income taxes   | 2,845                                |                 |
| (Gain) loss on early extinguishment or restructuring of debt  | (34,487)                             | 8,274           |
| Unrealized foreign currency transaction gain on intercompany and foreign debt                                   | (9,628)                              | (19,507)        |
| Changes in assets and liabilities, net of acquisitions:   |                                      |                 |
| (Increase) decrease in accounts receivable  | (6,388)                              | 1,028           |
| Decrease in prepaid expenses and other current assets   | 11,234                               | 2,053           |
| (Increase) decrease in other assets   | 905                                  | (106)           |
| Decrease in accounts payable  | (16,639)                             | (556)           |
| Increase (decrease) in accrued interconnection costs  | 3,159                                | (4,645)         |
| Increase (decrease) in accrued expenses, deferred revenue, other current liabilities and other liabilities, net | (3,079)                              | 929             |
| Decrease in accrued income taxes  | (4,455)                              | (4,844)         |
| Decrease in accrued interest  | (921)                                | (1,029)         |
| <b>Net cash provided by operating activities</b>  | <b>5,303</b>                         | <b>5,308</b>    |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>  |                                      |                 |
| Purchase of property and equipment  | (14,599)                             | (17,041)        |
| Sale of property and equipment  | 805                                  |                 |
| Cash from disposition of business, net of cash disposed   | 1,676                                | 5,527           |
| Cash used in business acquisitions, net of cash acquired  | (34)                                 |                 |
| Decrease in restricted cash   | 103                                  | 596             |
| <b>Net cash used in investing activities</b>  | <b>(12,049)</b>                      | <b>(10,918)</b> |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>  |                                      |                 |
| Purchase of the Company's debt securities   | (11,217)                             |                 |
| Proceeds from issuance of long-term obligations   |                                      | 109,275         |
| Deferred financing costs  |                                      | (6,570)         |
| Principal payments on long-term obligations   | (8,287)                              | (58,179)        |
| <b>Net cash provided by (used in) financing activities</b>  | <b>(19,504)</b>                      | <b>44,526</b>   |
| <b>EFFECTS OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>  | <b>518</b>                           | <b>1,451</b>    |
| <b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>  | <b>(25,732)</b>                      | <b>40,367</b>   |



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|   |              |            |
|---|--------------|------------|
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD                          | 81,282       | 64,317     |
| CASH AND CASH EQUIVALENTS, END OF PERIOD                                | \$ 55,550    | \$ 104,684 |
| SUPPLEMENTAL CASH FLOW INFORMATION:                                     |              |            |
| Cash paid for interest  | \$ 28,440    | \$ 29,776  |
| Cash paid for taxes   | \$ 469       | \$ 669     |
| Non-cash investing and financing activities:                            |              |            |
| Capital lease additions   | \$ 35        | \$ 1,981   |
| Leased fiber capacity additions   | \$           | \$ 1,786   |
| Settlement of outstanding debt with issuance of common stock            | \$           | \$ 6,627   |
| Settlement of outstanding debt with issuance of new senior secured debt | \$ (133,159) | \$         |
| Issuance of new senior secured debt in exchange for outstanding debt    | \$ 88,794    | \$         |
| Business disposition proceeds in note receivable                        | \$           | \$ 641     |

See notes to consolidated financial statements.

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**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**  
**CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME**

(in thousands)

(unaudited)

|   | Three Months Ended<br>June 30, |           | Six Months Ended<br>June 30, |          |
|---|--------------------------------|-----------|------------------------------|----------|
|   | 2008                           | 2007      | 2008                         | 2007     |
| NET INCOME                              | \$ 46,524                      | \$ 12,101 | \$ 43,525                    | \$ 9,459 |
| OTHER COMPREHENSIVE LOSS                |                                |           |                              |          |
| Foreign currency translation adjustment | (3,021)                        | (6,795)   | (4,048)                      | (8,411)  |
| COMPREHENSIVE INCOME                    | \$ 43,503                      | \$ 5,306  | \$ 39,477                    | \$ 1,048 |

See notes to consolidated financial statements.

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**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**

**NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**

**(UNAUDITED)**

**1. BASIS OF PRESENTATION**

The accompanying unaudited consolidated condensed financial statements of Primus Telecommunications Group, Incorporated and subsidiaries (the Company or Primus ) have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial reporting and Securities and Exchange Commission ( SEC ) regulations. Certain information and footnote disclosures normally included in the financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such principles and regulations. In the opinion of management, the financial statements reflect all adjustments (all of which are of a normal and recurring nature), which are necessary to present fairly the financial position, results of operations, cash flows and comprehensive income (loss) for the interim periods. The results for the three or six months ended June 30, 2008 are not necessarily indicative of the results that may be expected for the year ending December 31, 2008.

The results for the three months and six months ended June 30, 2008 and June 30, 2007 reflect the activities of certain operations as discontinued operations (see Note 10 Discontinued Operations ).

The financial statements should be read in conjunction with the Company s audited consolidated financial statements included in the Company s most recently filed Form 10-K.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Liquidity Outlook* As of June 30, 2008, the Company has \$55.6 million of cash and cash equivalents. The Company believes that its existing cash and cash equivalents, will be sufficient to fund its debt service requirements, other fixed obligations (such as capital leases, vendor financing and other long-term obligations), and other cash needs for its operations for at least the next twelve months. The Company will continue to have significant debt service obligations on a mid-term and a long-term basis, as disclosed in Note 4. After recent debt buybacks and exchanges, the Company has \$14.2 million principal amount of 12<sup>3</sup>/<sub>4</sub>% Senior Notes due in October 2009 and \$8.6 million principal amount of Step Up Convertible Subordinated Debentures coming due in August 2009. The Company s strategies related to meeting its 2009 obligations and other cash needs are to strengthen the balance sheet opportunistically through potential de-leveraging transactions and equity capital infusions; to improve the non-sales and marketing cost structure and maintain an aggressive cost management program; to focus on improving sales productivity and margin enhancements by leveraging the network assets and increasing the revenue mix in favor of higher margin growth services; and opportunistically to sell non-strategic assets and businesses and use the proceeds either to accelerate increases in high margin products or to reduce debt. Although the Company believes that it will have sufficient liquidity to fund its obligations for the next 12 months, there can be no assurance that the Company will be successful in implementing its longer term strategies or obtain new capital at acceptable terms.

*Principles of Consolidation* The consolidated financial statements include the Company s accounts, its wholly-owned subsidiaries and all other subsidiaries over which the Company exerts control. All intercompany profits, transactions and balances have been eliminated in consolidation. Beginning in the second quarter 2008, the Company intended and had the authority to sell its German retail operations, and therefore, is reporting this unit as discontinued operations. In March 2008, the Company sold its minority equity interest in Bekkoame Internet, Inc. ( Bekko ). The Company used the equity method of accounting for its investment in Bekko.

*Presentation of sales taxes collected* The Company reports any tax assessed by a governmental authority that is directly imposed on a revenue-producing transaction between the Company and a customer (including sales, use, value-added and some excise taxes) on a net basis (excluded from revenues).

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*Stock-Based Compensation* The Company uses a Black-Scholes option valuation model to determine the fair value of stock-based compensation under Statement of Financial Accounting Standards (SFAS) No. 123(R), consistent with that used for pro forma disclosures under SFAS No. 123. The Black-Scholes model incorporates various assumptions including the expected term of awards, volatility of stock price, risk-free rates of return and dividend yield. The expected term of an award is no less than the option vesting period and is based on the Company's historical experience. Expected volatility is based upon the historical volatility of the Company's stock price. The risk-free interest rate is approximated using rates available on U.S. Treasury securities with a remaining term similar to the option's expected life. The Company uses a dividend yield of zero in the Black-Scholes option valuation model as it does not anticipate paying cash dividends in the foreseeable future. The Company also had an Employee Stock Purchase Plan, which was suspended on July 27, 2006, and which allowed employees to elect to purchase stock at 85% of fair market value (determined monthly) and was considered compensatory under SFAS No. 123(R).

The Company recorded an incremental \$70 thousand and \$132 thousand stock-based compensation expenses for the three and six months ended June 30, 2008, respectively, and an incremental \$67 thousand and \$125 thousand during the three months and six months ended June 30, 2007, respectively, under guidance in SFAS No. 123(R).

The Company granted 125,000 and 90,000 options during the three months ended June 30, 2008 and 2007, respectively. The weighted average fair value at date of grant for options granted during the three months ended June 30, 2008 and 2007 was \$0.10 and \$0.32 per option, respectively. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

|                                 | For the Three<br>Months Ended<br>June 30, |         |
|---------------------------------|---|---------|
|                                 | 2008                                      | 2007    |
| Expected dividend yield         | 0%  | 0%      |
| Expected stock price volatility | 96%                                       | 95%     |
| Risk-free interest rate         | 3.0%                                      | 5.0%    |
| Expected option term            | 4 years                                   | 4 years |

As of June 30, 2008, the Company had 1.5 million unvested awards outstanding of which \$0.2 million of compensation expense will be recognized over the weighted average remaining vesting period of 2.14 years.

*Use of Estimates* The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions. These estimates and assumptions affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of net revenue and expenses during the reporting period. Actual results may differ from these estimates. Significant estimates include allowance for doubtful accounts receivable, accrued interconnection cost disputes, the fair value of embedded derivatives, market assumptions used in estimating the fair values of certain assets and liabilities such as marketable securities and long-term obligations, the calculation used in determining the fair value of the Company's stock options required by SFAS No. 123(R), various tax contingencies, asset impairment write-downs, and purchase price allocations.

*Newly Adopted Accounting Principle*

Effective January 1, 2008, the Company adopted SFAS No. 157, Fair Value Measurements, for all financial instruments accounted for at fair value on a recurring basis. The Company does not have any non-financial instruments accounted for at fair value on a recurring basis. SFAS No. 157 establishes a new framework for measuring fair value and expands related disclosures. Broadly, the SFAS No. 157 framework requires fair value to be determined based on the exchange price that would be received for an asset or paid to

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transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants. SFAS No. 157 establishes market or observable inputs as the preferred source of values, followed by assumptions based on hypothetical transactions in the absence of market inputs.

The valuation techniques required by SFAS No. 157 are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect our market assumptions. These two types of inputs create the following fair value hierarchy:

Level 1: Quoted prices for identical instruments in active markets.

Level 2: Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

Level 3: Significant inputs to the valuation model are unobservable.

See table below for summary of the Company's financial instruments accounted for at fair value on a recurring basis:

|                  | June 30, 2008 | Fair Value as of June 30, 2008, using:                         |   |   |
|------------------|---------------|--|---|---|
|                  |               | Quoted prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Assets:          |               |  |   |   |
| Cash equivalents | \$ 14,538     | \$ 14,538  |   |   |
| Derivative       | 149           |  | \$ 149  |   |
| Total            | \$ 14,687     | \$ 14,538  | \$ 149  |   |

*New Accounting Pronouncements*

In March 2008, the Financial Accounting Standard Board (FASB) issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities. SFAS No. 161 amends and expands the disclosure requirements of SFAS No. 133, Accounting for Derivative Instruments and Hedging with the intent to provide users of financial statements with an enhanced understanding of the use of derivative instruments, how derivative instruments and related hedged items are accounted for, and how derivative instruments and related hedged items affect an entity's financial statements. SFAS No. 161 is effective for financial statements issued for fiscal years after July 1, 2009. The Company anticipates that the adoption of this standard will not have a material impact on its results of operations, financial position and cash flows.

**3. GOODWILL AND OTHER INTANGIBLE ASSETS**

Acquired intangible assets subject to amortization consisted of the following (in thousands):

|                | As of June 30, 2008   |                          |                | As of December 31, 2007 |                          |                |
|----------------|-----------------------|--------------------------|----------------|-------------------------|--------------------------|----------------|
|                | Gross Carrying Amount | Accumulated Amortization | Net Book Value | Gross Carrying Amount   | Accumulated Amortization | Net Book Value |
| Customer lists | \$ 4,225              | \$ (3,418)               | \$ 807         | \$ 4,074                | \$ (2,688)               | \$ 1,386       |
| Other          | 1,884                 | (1,702)                  | 182            | 1,678                   | (1,507)                  | 171            |

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|       |          |            |        |          |            |          |
|-------|----------|------------|--------|----------|------------|----------|
| Total | \$ 6,109 | \$ (5,120) | \$ 989 | \$ 5,752 | \$ (4,195) | \$ 1,557 |
|-------|----------|------------|--------|----------|------------|----------|

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Amortization expense for customer lists and other intangible assets for the three months ended June 30, 2008 and 2007 was \$0.5 million and \$1.0 million, respectively. Amortization expense for customer lists and other intangible assets for the six months ended June 30, 2008 and 2007 was \$1.0 million and \$1.5 million, respectively. The Company expects amortization expense for customer lists and other intangible assets for the remainder of 2008 and the year ended December 31, 2009 to be approximately \$0.7 million and \$0.3 million, respectively.

Acquired intangible assets not subject to amortization consisted of the following (in thousands):

|          | <b>As of<br/>June 30,<br/>2008</b> | <b>As of<br/>December 31,<br/>2007</b> |
|----------|------------------------------------|--|
| Goodwill | \$ 40,539                          | \$ 40,134                              |

The changes in the carrying amount of goodwill for the six months ended June 30, 2008 are as follows (in thousands):

|   | <b>United States</b> | <b>Canada</b> | <b>Asia-Pacific</b> | <b>Total</b> |
|---|----------------------|---------------|---------------------|--------------|
| Balance as of January 1, 2008                       | \$ 208               | \$ 27,287     | \$ 12,639           | \$ 40,134    |
| Effect of change in foreign currency exchange rates | 21                   | (786)         | 1,170               | 405          |
| Balance as of June 30, 2008                         | \$ 229               | \$ 26,501     | \$ 13,809           | \$ 40,539    |

**4. LONG-TERM OBLIGATIONS**

Long-term obligations consisted of the following (in thousands):

|  | <b>June 30,<br/>2008</b> | <b>December 31,<br/>2007</b> |
|--|--------------------------|------------------------------|
| Obligations under capital leases               | \$ 6,776                 | \$ 7,350                     |
| Leased fiber capacity                          | 4,760                    | 5,201                        |
| Senior secured term loan facility              | 96,750                   | 97,250                       |
| Financing facility                             | 35,000                   | 35,000                       |
| Senior notes                                   | 200,186                  | 255,270                      |
| Senior secured notes                           | 206,744                  | 113,947                      |
| Exchangeable senior notes                      | 25,706                   | 63,363                       |
| Convertible senior notes                       | 33,954                   | 76,196                       |
| Step up convertible subordinated debentures    | 8,301                    | 20,326                       |
| Subtotal                                       | 618,177                  | 673,903                      |
| Less: Current portion of long-term obligations | (9,301)                  | (11,228)                     |
| Total long-term obligations                    | \$ 608,876               | \$ 662,675                   |

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Payments of principal and interest are due as follows:

| Year Ending December 31,   | Vendor<br>Financing | Senior<br>Secured<br>Term Loan<br>Facility (1) | Financing<br>Facility | Senior<br>Notes   | Convertible<br>and<br>Exchangeable<br>Senior Notes (2) | Step Up<br>Convertible<br>Subordinated<br>Debentures | Senior<br>Secured<br>Notes (2) | Total             |
|--|---------------------|--|-----------------------|-------------------|--|--|--------------------------------|-------------------|
| 2008 (as of June 30, 2008)   | \$ 5,477            | \$ 5,234                                       | \$ 1,562              | \$ 8,344          | \$ 1,225   | \$ 346   | \$ 13,486                      | \$ 35,674         |
| 2009   | 3,550               | 10,396   | 3,124                 | 30,875            | 2,451  | 9,332  | 24,980                         | 84,708            |
| 2010   | 3,327               | 10,298   | 3,124                 | 14,880            | 59,436   |  | 24,980                         | 116,045           |
| 2011   | 75                  | 94,250   | 3,124                 | 14,880            |  |  | 186,789                        | 299,118           |
| 2012   | 44                  |  | 35,781                | 14,880            |  |  |                                | 50,705            |
| Thereafter   | 62                  |  |                       | 208,320           |  |  |                                | 208,382           |
| <b>Total Minimum Principal &amp; Interest<br/>Payments</b>   | <b>12,535</b>       | <b>120,178</b>                                 | <b>46,715</b>         | <b>292,179</b>    | <b>63,112</b>  | <b>9,678</b>   | <b>250,235</b>                 | <b>794,632</b>    |
| Less: Amount Representing Interest   | (999)               | (23,428)                                       | (11,715)              | (91,993)          | (5,543)  | (1,037)  | (74,934)                       | (209,649)         |
| <b>Face Value of Long-Term<br/>Obligations</b>   | <b>11,536</b>       | <b>96,750</b>                                  | <b>35,000</b>         | <b>200,186</b>    | <b>57,569</b>  | <b>8,641</b>   | <b>175,301</b>                 | <b>584,983</b>    |
| Amount Representing Premium<br>(Discount)  |                     |  |                       |                   | (246)  | (340)  | 5,038                          | 4,452             |
| <b>Add: Exchangeable Senior Notes and<br/>Senior Secured Notes Interest<br/>Treated as Long-Term Obligations</b> |                     |  |                       |                   | <b>2,337</b>   |  | <b>26,405</b>                  | <b>28,742</b>     |
| <b>Book Value of Long Term<br/>Obligations</b>   | <b>\$ 11,536</b>    | <b>\$ 96,750</b>                               | <b>\$ 35,000</b>      | <b>\$ 200,186</b> | <b>\$ 59,660</b>                                       | <b>\$ 8,301</b>                                      | <b>\$ 206,744</b>              | <b>\$ 618,177</b> |

- (1) For preparation of this table, the Company has assumed the interest rate of the Senior Secured Term Loan Facility to be 9.8%, which is the interest rate at June 30, 2008.
- (2) For preparation of this table, the Company has shown separately the cash interest payments of the 5% Exchangeable Senior Notes and the portion of the 14 1/4% Senior Secured Notes that were issued through troubled debt restructurings as a portion of long-term obligations (see *Senior Notes, Senior Secured Notes, Convertible Senior Notes, Exchangeable Senior Notes, Step Up Convertible Subordinated Debentures and Convertible Subordinated Debentures* below). The interest due on the 5% Exchangeable Senior Notes in 2008, 2009 and 2010 is \$0.6 million, \$1.2 million and \$0.6 million, respectively. The interest due on this portion of the 14 1/4% Senior Secured Notes in 2008, 2009, 2010 and 2011 is \$5.4 million, \$8.8 million, \$8.8 million and \$3.4 million, respectively.

The indentures governing the senior notes, senior secured notes, senior secured term loan facility, convertible and exchangeable senior notes, and step up convertible subordinated debentures, as well as other credit arrangements, contain certain financial and other covenants which, among other things, will restrict the Company's ability to incur further indebtedness and make certain payments, including the payment of dividends and repurchase of subordinated debt held by the Company. The Company was in compliance with the above covenants at June 30, 2008.

**Senior Secured Term Loan Facility**

In February 2005, a direct wholly-owned subsidiary of the Company, Primus Telecommunications Holding, Inc. (PTHI), entered into a six-year, \$100 million senior secured term loan facility (the Facility). Each borrowing made under the Facility may be, at the election of PTHI at the time of the borrowing, a London Inter-Bank Offered Rate (LIBOR) loan (which will bear interest at a rate equal to LIBOR + 6.50%), or a base rate loan (which will bear interest at a rate equal to the greater of the prime rate plus 5.50% or the federal funds effective rate plus 6.0%). The Facility contains no financial maintenance covenants. The Company borrowed \$100 million under this Facility in February 2005.





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The Facility is to be repaid in 24 quarterly installments, which began on June 30, 2005, at a rate of one percent of the original principal per year over the next five years and nine months, and the remaining balance repaid on the sixth anniversary date of the Facility, with early redemption at a premium to par at PTHI's option at any time after February 18, 2006. The Facility is guaranteed by the Company and certain of PTHI's subsidiaries and is secured by certain assets of PTHI and its guarantor subsidiaries and stock pledges.

In February 2007, the Company received unanimous consent to an amendment of its existing \$100 million Facility. This amendment enables Primus Telecommunications IHC, Inc. (IHC), a wholly-owned indirect subsidiary of the Company, to issue and have at any one time outstanding up to \$200 million of existing authorized indebtedness in the form of newly authorized secured notes with a second lien security position. Pursuant to this authorization, the Company has issued certain secured second lien notes ( 1<sup>3</sup>/<sub>4</sub> % Senior Secured Notes ). The amendment allowed for an increase of 1/4% to the interest rate of the Facility and adjusted the early call features.

The effective interest rate for the Facility at June 30, 2008 was 9.8%.

**Financing Facility**

In March 2007, the Company entered into a Senior Secured Credit Agreement ( Credit Agreement ) with a financial institution, to refinance an existing Canadian credit facility. The Credit Agreement provides for a \$35.0 million non-amortizing loan bearing interest at a rate of LIBOR plus 425 basis points and matures in March 2012. The loan proceeds were used to refinance the existing Canadian credit facility, including certain costs related to the transaction, and to finance certain capital expenditures. The Credit Agreement is secured by the assets of the Company's Canadian operations and certain guarantees. In October 2007, the Company entered into a cross-currency principal and interest rate swap agreement, a portion of which was required by the Credit Agreement, which fixed the interest rate at 9.21% starting from October 31, 2007. At June 30, 2008, the Company had an outstanding liability of \$35.0 million.

*Senior Notes, Senior Secured Notes, Convertible Senior Notes, Exchangeable Senior Notes, Step Up Convertible Subordinated Debentures and Convertible Subordinated Debentures*

*14<sup>1</sup>/<sub>4</sub>% Senior Secured Notes*

In February 2007, subsequent to the effectiveness of the amendment of the Facility, IHC issued in a private transaction \$57.2 million principal amount of the 14<sup>1</sup>/<sub>4</sub>% Senior Secured Notes in exchange for \$40.7 million principal amount of the Company's outstanding 12<sup>3</sup>/<sub>4</sub>% Senior Notes and \$23.6 million in cash. This exchange has been accounted for as a modification of debt with a portion deemed to be a troubled debt restructuring. In March 2007, IHC also issued for cash in private transactions an additional \$51.0 million principal amount of 14<sup>1</sup>/<sub>4</sub>% Senior Secured Notes with a \$0.3 million discount. Net cash proceeds from the 14<sup>1</sup>/<sub>4</sub>% Senior Secured Notes issuance, after giving effect to expenses, discounts and fees related to all of the foregoing transactions (including the amendment of the Facility) is \$69.2 million. The Company recorded \$5.1 million in costs associated with this issuance of the 14<sup>1</sup>/<sub>4</sub>% Senior Secured Notes, which have been recorded as a loss on restructuring of debt.

In May 2008, IHC issued \$67.1 million principal amount of the 14<sup>1</sup>/<sub>4</sub>% Senior Secured Notes in exchange for \$49.0 million principal amount of the Company's 8% senior notes due 2014 ( 8% Senior Notes ), \$33.0 million principal amount of the Company's 5% exchangeable senior notes due June 2010 ( 5% Exchangeable Senior Notes ), \$43.1 million principal amount of the Company's 3<sup>3</sup>/<sub>4</sub>% convertible senior notes due 2010 ( 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes ), \$5.3 million principal amount of the Company's 12<sup>3</sup>/<sub>4</sub>% senior notes due 2009 ( 12<sup>3</sup>/<sub>4</sub>% Senior Notes ), and \$4.7 million in cash. All exchanges were deemed troubled debt restructurings, and accordingly, have been accounted for as modifications of debt, with future cash interest payments of \$26.4 million being recorded in long-term obligations. The Company recognized a gain on restructuring of debt of \$32.2 million in connection with this exchange, including the expensing of \$0.5 million of financing costs.

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The 14 1/4% Senior Secured Notes will mature on May 20, 2011 with early redemption at a premium to par at IHC's option at any time after February 2008. During specified periods, IHC may redeem at par up to 35% of the aggregate principal amount of the 14 1/4% Senior Secured Notes with the net cash proceeds of certain equity offerings of the Company. Accrued interest will be paid each May 31<sup>st</sup> and November 30<sup>th</sup>, beginning May 31<sup>st</sup>, 2007. The effective interest rate for the 14 1/4% Senior Secured Notes at June 30, 2008 was 12.4% for those amounts not related to the troubled debt restructuring discussed above (see Note 12 Guarantor/Non-Guarantor Consolidating Condensed Financial Information. )

*5% Exchangeable Senior Notes*

In the second quarter 2006, the Company completed the exchange of \$54.8 million principal amount of the Company's 3/4% Convertible Senior Notes and \$20.5 million in cash for \$56.3 million principal amount of PTHI's 5% Exchangeable Senior Notes. This exchange was deemed a troubled debt restructuring, and accordingly, has been accounted for as a modification of debt, with total future cash payments of \$67.6 million being recorded in long-term obligations. The Company recognized a gain on restructuring of debt of \$4.8 million in connection with this exchange, including the expensing of \$2.9 million of financing costs.

The 5% Exchangeable Senior Notes mature on June 30, 2010, as a result of the Company increasing its equity (through designated transactions) in the aggregate of \$25 million during June and July 2007. Interest on the 5% Exchangeable Senior Notes is paid at the rate of 5% per annum on each June 30 and December 30, beginning on December 30, 2006. Under certain circumstances, the Company may elect to make interest payments in shares of common stock, although the holders of the 5% Exchangeable Senior Notes were entitled to receive the first two semi-annual interest payments wholly in cash. The 5% Exchangeable Senior Notes are exchangeable, in the aggregate, into 19,474,167 shares of the Company's common stock at a conversion price of \$1.20 per share of common stock, subject to adjustment. If the closing bid price of the Company's common stock, for at least 20 trading days in any consecutive 30 trading-day period, exceeds 150% of the conversion price then in effect, the Company may elect to exchange the senior notes for shares of the Company's common stock at the conversion price, subject to certain conditions, including that no more than 50% of the 5% Exchangeable Senior Notes may be exchanged by the Company within any 30-day period. As of June 30, 2008, such conversion trigger had not been met. In the event of a change in control, as defined, the holders may require the Company to repurchase the 5% Exchangeable Senior Notes at which time the Company has the option to settle in cash or common stock at an adjusted conversion price. The 5% Exchangeable Senior Notes are guaranteed by Primus Telecommunications Group, Incorporated (PTGI) (see Note 12 Guarantor/Non-Guarantor Consolidating Condensed Financial Information ).

In May 2008, the Company restructured \$33.0 million principal amount of the 5% Exchangeable Senior Notes; see prior disclosure regarding the 14 1/4% Senior Secured Notes within this footnote.

*Step Up Convertible Subordinated Debentures*

In the first quarter 2006, the Company completed the exchange of \$27.4 million principal amount of the Company's 3/4% convertible subordinated debentures due 2007 ( 2000 Convertible Subordinated Debentures ) for \$27.5 million principal amount of the Company's step up convertible subordinated debentures due August 2009 ( Step Up Convertible Subordinated Debentures ) through two transactions. The Company recognized a gain on early extinguishment of debt of \$1.5 million in connection with this exchange.

The Step Up Convertible Subordinated Debentures will mature on August 15, 2009. Interest will be payable from February 27, 2006 to December 31, 2006 at the rate of 6% per annum; from January 1, 2007 to December 31, 2007 at the rate of 7% per annum; and from January 1, 2008 to maturity at the rate of 8% per annum. Accrued interest will be paid each February 15 and August 15, beginning August 15, 2006, to holders of record on the preceding February 1 and August 1, respectively. The Step Up Convertible Subordinated Debentures are convertible into the Company's common stock at a conversion price of \$1.187 per share of common stock through August 15, 2009. The Indenture permits the Company, at its sole option, to require

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conversion if the Company's stock trades at 150% of the conversion price for at least 20 days within a 30 day period, subject to certain conditions, including that no more than 25% of the notes may be exchanged within any 30 day trading period. As of June 30, 2008, such conversion trigger had not been met. In the event of a change in control, as defined, the holders may put the instrument to the Company at which time the Company has the option to settle in cash or common stock at an adjusted conversion price.

During the quarter ended June 30, 2007, the Company exchanged 6,000,000 shares of the Company's common stock for the extinguishment of \$5.0 million in principal amount of these convertible subordinated debentures. In accordance with SFAS No. 84, Induced Conversion of Convertible Debt, the Company recognized an induced conversion expense of \$1.6 million and \$0.7 million write-off of debt discount and deferred financing costs in connection with this conversion. During the first quarter of 2008, the Company made open market purchases of \$13.8 million principal amount of its Step Up Convertible Subordinated Debentures, resulting in a \$2.1 million gain on early extinguishment of debt including the write-off of related deferred financing costs. The outstanding Step Up Convertible Subordinated Debentures are convertible in the aggregate into 7,279,697 shares of the Company's common stock.

*Step Up Convertible Subordinated Debentures and 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes Supplemental Information*

At the time of issuance of the Step Up Convertible Subordinated Debentures, the Company did not have sufficient authorized and unissued shares of common stock to satisfy exercise and conversion of all of its convertible instruments. Accordingly, the Company determined that the Step Up Convertible Subordinated Debentures, the 2000 Convertible Subordinated Debentures and the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes were hybrid instruments with characteristics of a debt host agreement and contained embedded derivative features that had characteristics and risks that were not clearly and closely associated with the debt host. In the first quarter 2006, the conversion options were determined to be derivative instruments to be bifurcated and recorded as a current liability at fair value. In the second quarter 2006, the Company's shareholders voted to approve alternative proposals to authorize an amendment to the Company's Certificate of Incorporation to affect a one-for-ten reverse stock split or to authorize an amendment of the Company's Certificate of Incorporation allowing an increase of authorized common stock from 150,000,000 to 300,000,000. Either authorization ensured the Company would have the ability to control whether it has sufficient authorized and unissued shares of common stock to satisfy exercise and conversion of all of its convertible instruments. Therefore, the Company determined that the Step Up Convertible Subordinated Debentures, the 2000 Convertible Subordinated Debentures and the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes did not contain embedded derivative features as of the date of the shareholder vote, June 20, 2006, and added back the June 20, 2006 fair value of the embedded derivative into the debt balance. On July 27, 2006, the Board of Directors determined to increase the authorized shares of the common stock to 300,000,000.

The Company recorded a corresponding debt discount to the Step Up Convertible Subordinated Debentures and the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes in the amount of the fair value of the embedded derivative at the issue date. An additional debt discount of \$1.7 million was recorded for the Step Up Convertible Subordinated Debentures to bring the carrying value to fair value. The carrying value of the Step Up Convertible Subordinated Debentures at issuance was approximately \$14.3 million, and the carrying value of the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes at issuance of the Step Up Convertible Subordinated Debentures was approximately \$127.8 million. The Company is accreting the difference between the face values of the Step Up Convertible Subordinated Debentures and the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes and the corresponding carrying values to interest expense under the effective interest method on a monthly basis over the lives of the Step Up Convertible Subordinated Debentures and the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes. At June 30, 2008, the carrying value of the Step Up Convertible Subordinated Debentures (face value of \$8.6 million) was \$8.3 million, and the carrying value of the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes (face value of \$34.2 million) was \$34.0 million. The effective interest rates of the Step Up Convertible Subordinated Debentures and the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes at June 30, 2008 were 11.1% and 7.3%, respectively.

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*8% Senior Notes*

In January 2004, PTHI, a direct, wholly-owned subsidiary of the Company, completed the sale of \$240 million in aggregate principal amount of 8% Senior Notes with semi-annual interest payments due on January 15<sup>th</sup> and July 15<sup>th</sup>, with early redemption at a premium to par at PTHI's option at any time after January 15, 2009. The Company recorded \$6.7 million in costs associated with the issuance of the 8% Senior Notes, which have been recorded as deferred financing costs in other assets. The effective interest rate at June 30, 2008 was 8.4%. During specified periods, PTHI may redeem up to 35% of the original aggregate principal amount with the net cash proceeds of certain equity offerings of the Company. The 8% Senior Notes are guaranteed by PTGI (see Note 12 – Guarantor/Non-Guarantor Consolidating Condensed Financial Information).

During the year ended December 31, 2004, the Company reduced \$5.0 million principal balance of the 8% Senior Notes through open market purchases. In May 2008, the Company restructured \$49.0 million principal amount of the 8% Senior Notes; see prior disclosure regarding the 14 1/4% Senior Secured Notes within this footnote.

*3 3/4% Convertible Senior Notes*

In September 2003, the Company completed the sale of \$132 million in aggregate principal amount of 3 3/4% Convertible Senior Notes. The 3 3/4% Convertible Senior Notes are due September 2010, with semi-annual interest payments due on March 15<sup>th</sup> and September 15<sup>th</sup>. The Company recorded \$5.2 million in costs associated with the issuance of the 3 3/4% Convertible Senior Notes, which have been recorded as deferred financing costs in other assets. Holders of these notes may convert their notes into the Company's common stock at any time prior to maturity at an initial conversion price of \$9.3234 per share, which is equivalent to an initial conversion rate of 107.257 shares per \$1,000 principal amount of the notes, subject to adjustment in certain circumstances. The outstanding notes are convertible in the aggregate into 3,668,190 shares of the Company's common stock. In the event of a change in control, as defined, the holders may put the instrument to the Company at which time the Company has the option to settle in cash or common stock at an adjusted conversion price.

In the second quarter 2006, the Company restructured \$54.8 million principal amount of 3 3/4% Convertible Senior Notes; see prior disclosure regarding the 5% Exchangeable Senior Notes within this footnote. In May 2008, the Company restructured \$43.1 million principal amount of 3 3/4% Convertible Senior Notes; see prior disclosure regarding the 14 1/4% Senior Secured Notes within this footnote.

*12 3/4% Senior Notes*

In October 1999, the Company completed the sale of \$250 million in aggregate principal amount of the 12 3/4% Senior Notes. The 12 3/4% Senior Notes are due October 15, 2009, with semi-annual interest payments due on October 15<sup>th</sup> and April 15<sup>th</sup> with early redemption at a premium to par at the Company's option at any time after October 15, 2004 and with an early redemption at par at the Company's option at any time after October 15, 2007.

During the years ended December 31, 2002, 2001 and 2000, the Company reduced the principal balance of these senior notes through open market purchases. In June and September 2002, the Company retired all of the 12 3/4% Senior Notes that it had previously purchased in the principal amount of \$134.3 million in aggregate. The retired principal had been held by the Company as treasury bonds and had been recorded as a reduction of long-term obligations. During the year ended December 31, 2004, the Company retired \$33.0 million principal amount of the 12 3/4% Senior Notes through open market purchases. During the year ended December 31, 2005, the Company exchanged 5,165,175 shares of the Company's common stock for the extinguishment of \$8.6 million principal amount of these senior notes. During the quarter ended March 31, 2006, the Company exchanged 1,825,000 shares of the Company's common stock for the extinguishment of \$2.5 million principal amount of these senior notes. During the first quarter 2007, the Company restructured \$40.7 million principal amount of the

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12<sup>3</sup>/<sub>4</sub>% Senior Notes; the Company entered into a supplemental indenture, amending the terms to eliminate certain covenants. See prior disclosure regarding the 14<sup>1</sup>/<sub>4</sub>% Senior Secured Notes within this footnote. During the remainder of 2007, the Company retired \$10.5 million principal amount of the 12<sup>3</sup>/<sub>4</sub>% Senior Notes through open market purchases. In the first quarter of 2008, the Company made open market purchases of \$0.8 million principal amount of its 12<sup>3</sup>/<sub>4</sub>% Senior Notes, resulting in a \$0.1 million gain on early extinguishment of debt including the write-off of related deferred financing costs. In May 2008, the Company restructured \$5.3 million principal amount of the 12<sup>3</sup>/<sub>4</sub>% Senior Notes; see prior disclosure regarding the 14<sup>1</sup>/<sub>4</sub>% Senior Secured Notes within this footnote.

**Leased Fiber Capacity**

In December 2000, the Company entered into a financing arrangement to purchase fiber optic capacity in Australia for 51.1 million Australian dollars (AUD) (\$28.5 million at December 31, 2000) from Optus Networks Pty. Limited. As of December 31, 2001, the Company had fulfilled the total purchase obligation. The Company signed a promissory note payable over a four-year term ending in April 2005 bearing interest at a rate of 14.31%. During the three months ended June 30, 2003, the Company renegotiated the payment terms extending the payment schedule through March 2007, and lowering the interest rate to 10.2%. In October 2006, the Company renegotiated the payment terms of its promissory note payable to Optus Networks Pty. Limited to defer principal payments from April 2006 through December 2006 and was obligated to pay the remaining balance in three equal monthly principal payments in the first quarter 2007. In February 2007, the Company again renegotiated the payment terms of its \$8.1 million (10.1 million AUD) promissory note payable to Optus Networks Pty. Limited to extend the payment schedule through December 2008 in 24 equal monthly payments. The interest rate remains 10.2%, and the interest payments continue monthly. At June 30, 2008 and December 31, 2007, the Company had a liability recorded in the amount of \$4.7 million (4.9 million AUD) and \$5.0 million (5.7 million AUD), respectively.

**Equipment Financing and Other Long-Term Obligations**

In November 2005, Primus Australia entered into a financing arrangement for network equipment. Payments are made over a five-year term ending October 2010. The effective interest rate on the current borrowing is 9.3%. At June 30, 2008 and December 31, 2007, the Company had a liability recorded under this agreement in the amount \$4.6 million (4.8 million AUD) and \$4.7 million (5.4 million AUD), respectively.

**5. COMMITMENTS AND CONTINGENCIES**

Future minimum lease payments under capital leases and leased fiber capacity financing ( Vendor Financing ), purchase obligations and non-cancelable operating leases as of June 30, 2008 are as follows (in thousands):

| Year Ending December 31,           | Vendor Financing | Purchase Obligations | Operating Leases |
|------------------------------------|------------------|----------------------|------------------|
| 2008 (as of June 30, 2008)         | \$ 5,477         | \$ 4,051             | \$ 7,960         |
| 2009                               | 3,550            | 7,503                | 13,089           |
| 2010                               | 3,327            | 3,316                | 10,018           |
| 2011                               | 75               | 2,584                | 7,288            |
| 2012                               | 44               | 1,587                | 5,692            |
| Thereafter                         | 62               |                      | 12,174           |
| Total minimum lease payments       | 12,535           | 19,041               | 56,221           |
| Less: Amount representing interest | (999)            |                      |                  |
|                                    | \$ 11,536        | \$ 19,041            | \$ 56,221        |

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The Company has contractual obligations to utilize an external vendor for certain customer support functions and to utilize network facilities from certain carriers with terms greater than one year. The Company does not purchase or commit to purchase quantities in excess of normal usage or amounts that cannot be used within the contract term or at rates below or above market value. The Company made purchases under purchase commitments of \$10.2 million and \$0.1 million for the three months ended June 30, 2008 and June 30, 2007, respectively. The Company made purchases under purchase commitments of \$19.1 million and \$0.1 million for the six months ended June 30, 2008 and 2007, respectively.

Rent expense under operating leases was \$4.7 million and \$4.6 million for the three months ended June 30, 2008 and 2007, respectively. Rent expense under operating leases was \$9.1 million and \$8.0 million for the six months ended June 30, 2008 and 2007, respectively.

### *Litigation*

The Company is subject to claims and legal proceedings that arise in the ordinary course of its business. Each of these matters is subject to various uncertainties, and it is possible that some of these matters may be decided unfavorably to the Company. The Company believes that any aggregate liability that may result from the resolution of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows. (See Note 2 Summary of Significant Accounting Policies ).

## **6. SHARE-BASED COMPENSATION**

The Company sponsors an employee stock compensation plan (the Equity Incentive Plan ). The total number of shares of common stock authorized for issuance under the Equity Incentive Plan is 13,000,000. Under the Equity Incentive Plan, awards may be granted to key employees or consultants of the Company and its subsidiaries in the form of Incentive Stock Options, Nonqualified Stock Options or Restricted Stock Units. The Equity Incentive Plan allows the granting of options at an exercise price of not less than 100% of the stock's fair value at the date of grant and allows the grant of restricted stock units (RSUs) for no consideration. The options and RSUs vest over a period of up to three years. No option will be exercisable more than ten years from the date it is granted. On June 16, 2004, the stockholders of the Company approved amendments to the Equity Incentive Plan, including (i) renaming the employee stock option plan the Equity Incentive Plan ; (ii) expanding the forms of awards permitted to be granted, including stock appreciation rights, restricted stock awards, stock units and other equity securities, and authorizing a tax deferral feature for executive officers; (iii) prohibiting the repricing of stock options in the future without stockholder approval; and (iv) requiring vesting in full to be not less than three years for restricted stock and stock unit awards, unless accelerated following the first anniversary of the award due to the satisfaction of predetermined performance conditions.

The Company sponsors a Director Stock Option Plan (the Director Plan ) for non-employee directors. Under the Director Plan, an option is granted to each qualifying non-employee director upon election or reelection to purchase 45,000 shares of common stock, which vests in one-third increments as of the grant date and the first and second anniversaries of the grant date, over a two-year period. The option price per share is the fair market value of a share of common stock on the date the option is granted. No option will be exercisable more than five years from the date of grant. On June 16, 2004, the stockholders of the Company approved amendments to the Director Plan to (i) increase the number of shares of common stock issuable pursuant to awards under the Director Plan by 300,000 to a total of 900,000; and (ii) authorize the issuance of restricted stock (in lieu of cash compensation at the discretion of individual Directors).

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A summary of stock option activity during the six months ended June 30 is as follows:

|                                      | 2008             |                                 | 2007             |                                 |
|--------------------------------------|------------------|---------------------------------|------------------|---------------------------------|
|                                      | Shares           | Weighted Average Exercise Price | Shares           | Weighted Average Exercise Price |
| Options outstanding January 1        | 7,368,262        | \$ 2.09                         | 7,919,267        | \$ 2.15                         |
| Granted                              | 1,035,000        | \$ 0.35                         | 90,000           | \$ 0.99                         |
| Exercised                            |                  | \$                              |                  | \$                              |
| Forfeitures                          | (333,693)        | \$ 2.52                         | (452,801)        | \$ 2.28                         |
| <b>Outstanding June 30</b>           | <b>8,069,569</b> | <b>\$ 1.86</b>                  | <b>7,556,466</b> | <b>\$ 2.13</b>                  |
| Eligible for exercise end of quarter | 6,637,527        | \$ 2.15                         | 6,587,349        | \$ 2.32                         |

The following table summarizes information about stock options outstanding at June 30, 2008:

| Range of Option Prices | Total Outstanding | Options Outstanding                      |                                 |                 | Total Exercisable | Options Exercisable                      |                                 |                 |
|------------------------|-------------------|--|---------------------------------|-----------------|-------------------|--|---------------------------------|-----------------|
|                        |                   | Weighted Average Remaining Life in Years | Weighted Average Exercise Price | Intrinsic Value |                   | Weighted Average Remaining Life in Years | Weighted Average Exercise Price | Intrinsic Value |
| \$0.27                 | 80,000            | 9.83                                     | \$ 0.27                         | \$ 5,600        |                   | 0.00                                     | \$                              | \$              |
| \$0.36 to \$0.65       | 1,173,167         | 8.79                                     | \$ 0.41                         | \$              | 182,500           | 4.86                                     | \$ 0.60                         | \$              |
| \$0.73 to \$0.88       | 724,333           | 7.20                                     | \$ 0.79                         | \$              | 515,997           | 7.00                                     | \$ 0.79                         | \$              |
| \$0.90                 | 757,321           | 3.02                                     | \$ 0.90                         | \$              | 757,321           | 3.02                                     | \$ 0.90                         | \$              |
| \$0.92                 | 772,080           | 7.36                                     | \$ 0.92                         | \$              | 649,041           | 7.36                                     | \$ 0.92                         | \$              |
| \$0.93 to \$0.99       | 110,000           | 4.64                                     | \$ 0.98                         | \$              | 80,000            | 4.89                                     | \$ 0.98                         | \$              |
| \$1.33 to \$1.61       | 19,500            | 5.31                                     | \$ 1.47                         | \$              | 19,500            | 5.31                                     | \$ 1.47                         | \$              |
| \$1.65                 | 1,477,773         | 4.47                                     | \$ 1.65                         | \$              | 1,477,773         | 4.47                                     | \$ 1.65                         | \$              |
| \$1.90 to \$2.38       | 1,716,045         | 4.50                                     | \$ 1.97                         | \$              | 1,716,045         | 4.50                                     | \$ 1.97                         | \$              |
| \$3.03 to \$6.30       | 1,214,500         | 6.09                                     | \$ 4.98                         | \$              | 1,214,500         | 6.09                                     | \$ 4.98                         | \$              |
| \$12.31 to \$17.44     | 16,800            | 1.02                                     | \$ 15.01                        | \$              | 16,800            | 1.02                                     | \$ 15.01                        | \$              |
| \$31.94                | 8,050             | 1.59                                     | \$ 31.94                        | \$              | 8,050             | 1.59                                     | \$ 31.94                        | \$              |
|                        | <b>8,069,569</b>  | <b>5.78</b>                              | <b>\$ 1.86</b>                  | <b>\$ 5,600</b> | <b>6,637,527</b>  | <b>5.09</b>                              | <b>\$ 2.15</b>                  | <b>\$</b>       |

The number of unvested options expected to vest is 0.6 million shares, with a weighted average remaining life of 9.0 years, a weighted average exercise price of \$0.47, and an intrinsic value of \$6 thousand.

In 2007, 100,000 restricted stock units were granted, which is the only grant to date. None have vested as their vesting schedule is to vest 100% three years from grant date. The fair market value of the stock units at the grant date was \$0.40 per share. In the second quarter of 2008, the Company recognized \$3 thousand expense related to this grant.

In December 1998, the Company established the 1998 Restricted Stock Plan (the Restricted Plan) to facilitate the grant of restricted stock to selected individuals (excluding executive officers and directors of the Company) who contribute to the development and success of the Company. The total number of shares of common stock that may be granted under the Restricted Plan is 750,000. The Company did not issue any restricted stock under the Restricted Plan for three months and six months ended June 30, 2008 and June 30, 2007. As of June 30, 2008, 54,000 shares have been issued, and none are considered restricted.





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**7. GAIN OR LOSS ON EARLY EXTINGUISHMENT OR RESTRUCTURING OF DEBT**

In May 2008, the Company exchanged \$49.0 million principal amount of the Company's 8% Senior Notes, \$33.0 million principal amount of the Company's 5% Exchangeable Senior Notes, \$43.1 million principal amount of the Company's 3/3% Convertible Senior Notes, \$5.3 million principal amount of the Company's 1 1/4% 1999 Senior Notes, and \$4.7 million of cash for \$67.1 million principal amount of the Company's 14 1/4% Senior Secured Notes, resulting in a gain on restructuring of debt of \$32.2 million including the expensing of \$0.5 million of related financing costs.

In the first quarter 2008, the Company made open market purchases of \$0.8 million of its 12 3/4% Senior Notes, resulting in a \$0.1 million gain on early extinguishment of debt including the write-off of related deferred financing costs.

In the first quarter 2008, the Company made open market purchases of \$13.8 million principal amount of its Step Up Convertible Subordinated Debentures, resulting in a \$2.1 million gain on early extinguishment of debt including the write-off of related deferred financing costs, discount and effective interest.

In June 2007, the Company exchanged 6,000,000 shares of the Company's common stock for the extinguishment of \$5.0 million principal amount of its Step Up Convertible Subordinated Debentures, resulting in a loss on early extinguishment of debt of \$2.3 million, including the write-off of related deferred financing costs and debt discount.

In March 2007, the Company refinanced an existing Canadian credit facility and recognized a \$0.9 million loss on early extinguishment of debt for pre-payment penalties and the write-off of related deferred financing costs.

In February 2007, IHC issued in a private transaction \$57.2 million principal amount of the 14 1/4% Senior Secured Notes, in exchange for \$40.7 million principal amount of the Company's outstanding 1 1/4% Senior Notes and \$23.6 million in cash. The Company recognized a loss on restructuring of debt of \$5.1 million in connection with this exchange.

**8. INCOME TAXES**

The Company conducts business globally, and as a result, the Company or one or more of its subsidiaries files income tax returns in the United States federal jurisdiction and various state and foreign jurisdictions. In the normal course of business we are subject to examination by taxing authorities throughout the world.

The following table summarizes the open tax years for each major jurisdiction:

| <b>Jurisdiction</b>   | <b>Open Tax Years</b> |
|-----------------------|-----------------------|
| United States Federal | 2000, 2002-2007       |
| Australia             | 2002-2007             |
| Canada                | 2003-2007             |
| United Kingdom        | 2002-2007             |
| Netherlands           | 2002-2007             |

During the second quarter of 2008 the Company concluded the Canadian audits for years 2000, 2001 and 2002. The final settlement of the audits resulted in a FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes, release of liability of \$3.2 million which impacted the effective rate. Upon conclusion of the prior year audits, Canada initiated audits for years 2004, 2005 and 2006 with expected completion during the first half of 2009. The Company is undergoing an examination in the Netherlands for the years 2002, 2003, 2004, and 2005 with an expected completion before year end 2008. The Company is also currently under examination in other foreign tax jurisdictions, none of which are individually material. As of June 30, 2008, \$104.0 million of unrecognized tax benefits have been recorded in accordance with FIN No. 48.

The Company adopted the provisions of FIN No. 48 on January 1, 2007. It is expected that the amount of unrecognized tax benefits, reflected in the Company's financial statements as a result of the adoption of

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FIN No. 48, will change in the next twelve months; however, the Company does not expect the change to have a significant impact on the results of operations or the financial position of the Company.

On an ongoing basis, the Company monitors activity in its 5% shareholder base for substantial changes in ownership as defined under Internal Revenue Code Section 382 ( Section 382 ). In 2007 and the rest of the testing periods under Section 382, the Company has had significant activity in this shareholder base, but upon review of the 13G filings and other available data the Company believes that an ownership change did not occur during 2007 or during the six months ended June 30, 2008. If a change is to occur, the resulting Section 382 limitation would place severe limits on the Company's ability to utilize the United States net operating losses.

**9. OPERATING SEGMENT AND RELATED INFORMATION**

The Company has five reportable operating segments based on management's organization of the enterprise into geographic areas: United States, Canada, Europe and Asia-Pacific, with the wholesale business within each region managed as a separate global segment. The Company evaluates the performance of its segments and allocates resources to them based upon net revenue and income (loss) from operations. The accounting policies of the segments are the same as those described in the summary of significant accounting policies. Net revenue by geographic segment is reported on the basis of where services are provided. The Company has no single customer representing greater than 10% of its revenues. Operations and assets of the United States segment include shared corporate functions and assets, which the Company does not allocate to its other geographic segments for management reporting purposes. The wholesale business' assets are indistinguishable from the respective geographic segments. Therefore, any reporting related to the wholesale business for assets, capital expenditures or other balance sheet items is impractical.

Summary information with respect to the Company's segments is as follows (in thousands):

|   | Three months ended<br>June 30, |                   | Six months ended<br>June 30, |                   |
|---|--------------------------------|-------------------|------------------------------|-------------------|
|   | 2008                           | 2007              | 2008                         | 2007              |
| <b>Net Revenue by Geographic Region</b> |                                |                   |                              |                   |
| United States                           |                                |                   |                              |                   |
| <i>United States</i>                    | \$ 42,505                      | \$ 42,887         | \$ 85,164                    | \$ 88,755         |
| <i>Other</i>                            | 2,680                          | 1,521             | 4,837                        | 2,666             |
| <b>Total United States</b>              | <b>45,185</b>                  | <b>44,408</b>     | <b>90,001</b>                | <b>91,421</b>     |
| Canada                                  |                                |                   |                              |                   |
| <i>Canada</i>                           | 68,989                         | 63,588            | 137,438                      | 126,372           |
| <b>Total Canada</b>                     | <b>68,989</b>                  | <b>63,588</b>     | <b>137,438</b>               | <b>126,372</b>    |
| Europe                                  |                                |                   |                              |                   |
| <i>United Kingdom</i>                   | 22,204                         | 25,100            | 39,581                       | 49,973            |
| <i>Germany</i>                          | 4,839                          | 5,200             | 9,746                        | 10,116            |
| <i>Other</i>                            | 18,618                         | 15,142            | 34,324                       | 30,265            |
| <b>Total Europe</b>                     | <b>45,661</b>                  | <b>45,442</b>     | <b>83,651</b>                | <b>90,354</b>     |
| Asia-Pacific                            |                                |                   |                              |                   |
| <i>Australia</i>                        | 75,992                         | 71,950            | 150,066                      | 142,151           |
| <i>Other</i>                            | 635                            | 1,042             | 1,384                        | 2,135             |
| <b>Total Asia-Pacific</b>               | <b>76,627</b>                  | <b>72,992</b>     | <b>151,452</b>               | <b>144,286</b>    |
| <b>Total net revenue</b>                | <b>\$ 236,462</b>              | <b>\$ 226,430</b> | <b>\$ 462,542</b>            | <b>\$ 452,433</b> |

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| <b>Net Revenue by Segment</b> |                   |                   |                   |                   |
|-------------------------------|-------------------|-------------------|-------------------|-------------------|
| United States                 | \$ 25,125         | \$ 28,352         | \$ 50,415         | \$ 55,745         |
| Canada                        | 68,989            | 63,500            | 137,438           | 126,160           |
| Europe                        | 16,925            | 18,431            | 32,690            | 38,472            |
| Asia-Pacific                  | 76,557            | 72,630            | 151,278           | 143,552           |
| Wholesale                     | 48,866            | 43,517            | 90,721            | 88,504            |
| <b>Total</b>                  | <b>\$ 236,462</b> | <b>\$ 226,430</b> | <b>\$ 462,542</b> | <b>\$ 452,433</b> |

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|   | Three months<br>ended June 30, |           | Six months ended<br>June 30, |            |
|---|--------------------------------|-----------|------------------------------|------------|
|   | 2008                           | 2007      | 2008                         | 2007       |
| <b>Provision for Doubtful Accounts Receivable</b> |                                |           |                              |            |
| United States                                     | \$ 831                         | \$ 131    | \$ 1,635                     | \$ 734     |
| Canada  | 531                            | 525       | 877                          | 1,281      |
| Europe  | 200                            | 238       | 398                          | 143        |
| Asia-Pacific                                      | 961                            | 946       | 2,228                        | 2,350      |
| Wholesale   | 345                            | 157       | 558                          | 381        |
| Total   | \$ 2,868                       | \$ 1,997  | \$ 5,696                     | \$ 4,889   |
| <b>Income (Loss) from Operations</b>              |                                |           |                              |            |
| United States                                     | \$ (1,970)                     | \$ (597)  | \$ (1,468)                   | \$ (3,942) |
| Canada  | 11,840                         | 9,919     | 23,365                       | 18,682     |
| Europe  | (2,007)                        | (3,218)   | (3,472)                      | (4,079)    |
| Asia-Pacific                                      | 7,931                          | 3,216     | 7,888                        | 6,986      |
| Wholesale   | (528)                          | (1,068)   | (1,296)                      | (1,669)    |
| Total   | \$ 15,266                      | \$ 8,252  | \$ 25,017                    | \$ 15,978  |
| <b>Capital Expenditures</b>                       |                                |           |                              |            |
| United States                                     | \$ 330                         | \$ 545    | \$ 690                       | \$ 829     |
| Canada  | 3,181                          | 5,029     | 5,323                        | 9,337      |
| Europe  | 214                            | 2,247     | 680                          | 2,529      |
| Asia-Pacific                                      | 4,017                          | 2,830     | 7,906                        | 4,346      |
| Total   | \$ 7,742                       | \$ 10,651 | \$ 14,599                    | \$ 17,041  |

The above capital expenditures exclude assets acquired under terms of capital lease and vendor financing obligations.

|                                   | June 30,<br>2008 | December 31,<br>2007 |
|-----------------------------------|------------------|----------------------|
| <b>Property and Equipment Net</b> |                  |                      |
| United States                     |                  |                      |
| <i>United States</i>              | \$ 16,731        | \$ 18,430            |
| <i>Other</i>                      | 693              | 597                  |
| Total United States               | 17,424           | 19,027               |
| Canada                            |                  |                      |
| <i>Canada</i>                     | 53,752           | 54,787               |
| Total Canada                      | 53,752           | 54,787               |
| Europe                            |                  |                      |
| <i>United Kingdom</i>             | 8,221            | 8,718                |
| <i>Germany</i>                    | 640              | 700                  |
| <i>Other</i>                      | 1,073            | 970                  |
| Total Europe                      | 9,934            | 10,388               |
| Asia-Pacific                      |                  |                      |

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|                           |               |               |
|---------------------------|---------------|---------------|
| <i>Australia</i>          | 66,484        | 60,233        |
| <i>Other</i>              | 159           | 164           |
| <b>Total Asia-Pacific</b> | <b>66,643</b> | <b>60,397</b> |
| Total                     | \$ 147,753    | \$ 144,599    |

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|                            | June 30,<br>2008  | December 31,<br>2007 |
|----------------------------|-------------------|----------------------|
| <b>Assets</b>              |                   |                      |
| United States              |                   |                      |
| <i>United States</i>       | \$ 41,687         | \$ 71,782            |
| <i>Other</i>               | 5,636             | 5,429                |
| <b>Total United States</b> | <b>47,323</b>     | <b>77,211</b>        |
| Canada                     |                   |                      |
| <i>Canada</i>              | 148,762           | 166,817              |
| <b>Total Canada</b>        | <b>148,762</b>    | <b>166,817</b>       |
| Europe                     |                   |                      |
| <i>United Kingdom</i>      | 28,117            | 21,434               |
| <i>Germany</i>             | 6,028             | 5,803                |
| <i>Other</i>               | 51,330            | 52,428               |
| <b>Total Europe</b>        | <b>85,475</b>     | <b>79,665</b>        |
| Asia-Pacific               |                   |                      |
| <i>Australia</i>           | 141,484           | 132,948              |
| <i>Other</i>               | 3,882             | 3,762                |
| <b>Total Asia-Pacific</b>  | <b>145,366</b>    | <b>136,710</b>       |
| <b>Total</b>               | <b>\$ 426,926</b> | <b>\$ 460,403</b>    |

The Company offers three main products voice, data/Internet and VOIP in all of its segments. Net revenue information with respect to the Company's products is as follows (in thousands):

|               | Three months ended<br>June 30, |                   | Six months ended<br>June 30, |                   |
|---------------|--------------------------------|-------------------|------------------------------|-------------------|
|               | 2008                           | 2007              | 2008                         | 2007              |
| Voice         | \$ 148,756                     | \$ 151,545        | \$ 292,513                   | \$ 304,308        |
| Data/Internet | 48,977                         | 44,870            | 96,392                       | 88,149            |
| VOIP          | 38,729                         | 30,015            | 73,637                       | 59,976            |
| <b>Total</b>  | <b>\$ 236,462</b>              | <b>\$ 226,430</b> | <b>\$ 462,542</b>            | <b>\$ 452,433</b> |

**10. DISCONTINUED OPERATIONS**

During the second quarter 2008, the Company determined to sell its German retail operations, and therefore, is reporting this unit as discontinued operations.

In August 2007, the Company sold its 51% interest in its German telephone installation system subsidiaries. The sale price was \$0.8 million (0.6 million Euros), which included \$0.5 million (0.4 million Euros) in cash and \$0.3 million (0.2 million Euros) for payment of outstanding intercompany debt. For the intercompany debt payment, the Company received \$0.1 million (0.1 million Euros) in cash at closing. The balance owing is represented by a note receivable and will be paid in fifteen equal monthly installment payments. As a result, the Company recorded a \$0.2 million gain from sale of assets. Net assets held for sale were \$0.6 million at the closing date.

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In February 2007, the Company sold its Australian domain name registry and web hosting subsidiary, Planet Domain. The sale price was \$6.5 million (\$8.3 million AUD). The Company received \$5.5 million in net cash proceeds from the transaction after closing adjustments. As a result, the Company recorded a \$6.0 million gain from sale of assets. The net assets of Planet Domain were \$0.2 million at the closing date.



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As a result of these events, the Company's consolidated financial statements reflect the German retail operations, discontinued German subsidiary and Planet Domain operations as discontinued operations for the three and six months ended June 30, 2008 and 2007. Accordingly, revenue, costs, and expenses of the discontinued operations have been excluded from the respective captions in the consolidated statements of operations. The net operating results of the discontinued operations have been reported, net of applicable income taxes as income from discontinued operations.

Summarized operating results of German retail operations, the discontinued German subsidiary and Planet Domain operations for the three and six months ended June 30, 2008 and 2007 are as follows (in thousands):

|                                   | Three Months<br>Ended June 30, |          | Six Months<br>Ended June 30, |          |
|-----------------------------------|--------------------------------|----------|------------------------------|----------|
|                                   | 2008                           | 2007     | 2008                         | 2007     |
| Net revenues                      | \$ 475                         | \$ 2,172 | \$ 996                       | \$ 4,726 |
| Operating expenses                | 566                            | 2,328    | 1,176                        | 4,979    |
| Loss from operations              | (91)                           | (156)    | (180)                        | (253)    |
| Interest expense                  |                                | (10)     |                              | (16)     |
| Interest income and other income  |                                |          |                              | 3        |
| Loss from discontinued operations | \$ (91)                        | \$ (166) | \$ (180)                     | \$ (266) |

**11. BASIC AND DILUTED INCOME (LOSS) PER COMMON SHARE**

Basic income (loss) per common share is calculated by dividing income (loss) attributable to common stockholders by the weighted average common shares outstanding during the period.

Diluted income per common share adjusts basic income per common share for the effects of potentially dilutive common share equivalents. Potentially dilutive common shares primarily include the dilutive effects of common shares issuable under the Company's stock option compensation plans computed using the treasury stock method and the dilutive effects of shares issuable upon conversion of its 5% Exchangeable Senior Notes, the Step Up Convertible Subordinated Debentures, the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes and the 2000 Convertible Subordinated Debentures.

For the three months ended June 30, 2008, the following could potentially dilute income per common share in the future but were excluded from the calculation of diluted income per common share due to their antidilutive effects:

8.0 million shares issuable upon exercise of stock options.

For the six months ended June 30, 2008, the following could potentially dilute income per common share in the future but were excluded from the calculation of diluted income per common share due to their antidilutive effects:

8.0 million shares issuable upon exercise of stock options, and

7.2 million shares issuable upon conversion of the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes.

For the three months ended June 30, 2007, the following could potentially dilute income per common share in the future but were excluded from the calculation of diluted income per common share due to their antidilutive effects:

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6.8 million shares issuable upon exercise of stock options, and

8.3 million shares issuable upon conversion of the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes.

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For the six months ended June 30, 2007, the following could potentially dilute income per common share in the future but were excluded from the calculation of diluted income per common share due to their antidilutive effects:

7.4 million shares issuable upon exercise of stock options,

8.3 million shares issuable upon conversion of the 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes, and

0.1 million shares issuable upon conversion of the 2000 Convertible Subordinated Debentures.

A reconciliation of basic income per common share to diluted income per common share is below (in thousands, except per share amounts):

|   | Three months ended<br>June 30, |           | Six months ended<br>June 30, |           |
|---|--------------------------------|-----------|------------------------------|-----------|
|   | 2008                           | 2007      | 2008                         | 2007      |
| Income from continuing operations   | \$ 46,615                      | \$ 12,267 | \$ 43,705                    | \$ 3,767  |
| Loss from discontinued operations, net of tax   | (91)                           | (166)     | (180)                        | (266)     |
| Gain from sale of discontinued operations, net of tax                                       |                                |           |                              | 5,958     |
| Income attributable to common stockholders basic  | 46,524                         | 12,101    | 43,525                       | 9,459     |
| Adjustment for interest expense on Step Up Convertible Subordinated Debentures              | 231                            | 477       | 874                          | 976       |
| Adjustment for interest expense on 3 <sup>3</sup> / <sub>4</sub> % Convertible Senior Notes | 741                            |           |                              |           |
| Income attributable to common stockholders diluted  | \$ 47,496                      | \$ 12,578 | \$ 44,399                    | \$ 10,435 |
| Weighted average common shares outstanding basic  | 142,633                        | 115,715   | 142,633                      | 114,928   |
| In-the-money options exercisable under stock option compensation plans                      |                                | 27        |                              | 10        |
| 5% Exchangeable Senior Notes  | 34,261                         | 46,936    | 40,598                       | 46,936    |
| Step Up Convertible Subordinated Debentures   | 7,280                          | 22,041    | 11,990                       | 22,593    |
| 3 <sup>3</sup> / <sub>4</sub> % Convertible Senior Notes                                    | 6,154                          |           |                              |           |
| Weighted average common shares outstanding diluted  | 190,328                        | 184,719   | 195,221                      | 184,467   |
| Basic income (loss) per common share:   |                                |           |                              |           |
| Income from continuing operations   | \$ 0.33                        | \$ 0.11   | \$ 0.31                      | \$ 0.03   |
| Loss from discontinued operations   | (0.00)                         | (0.01)    | (0.00)                       | (0.00)    |
| Gain from sale of discontinued operations   |                                |           |                              | 0.05      |
| Net income  | \$ 0.33                        | \$ 0.10   | \$ 0.31                      | \$ 0.08   |
| Diluted income (loss) per common share:   |                                |           |                              |           |
| Income from continuing operations   | \$ 0.25                        | \$ 0.07   | \$ 0.23                      | \$ 0.02   |
| Loss from discontinued operations   | (0.00)                         | (0.00)    | (0.00)                       | (0.00)    |
| Gain from sale of discontinued operations   |                                |           |                              | 0.04      |
| Net income  | \$ 0.25                        | \$ 0.07   | \$ 0.23                      | \$ 0.06   |



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**12. GUARANTOR/NON-GUARANTOR CONDENSED CONSOLIDATED FINANCIAL INFORMATION**

Subsequent to the issuance of the 2007 consolidated financial statements, the Company determined that its 2007 disclosures of consolidating financial information incorrectly excluded the intercompany interest and related accrued intercompany receivables and payables that resulted from three intercompany loans between IHC, PTGI and PTHI. The effects of this correction on the 2007 consolidating condensed financial statements are shown in the table below. The consolidating condensed statements of operations for the three months and six months ended June 30, 2007, the consolidating condensed statements of cash flows for the six months ended June 30, 2007, and the consolidating condensed balance sheets at December 31, 2007 contained herein have been restated to include the effects of the adjustments shown in the tables below as increases (decreases) in the effected line items to reflect correctly intercompany interest charged by IHC to PTGI and PTHI on intercompany notes issued in 2007. The effects of this correction on the consolidating condensed statements of operations and cash flows for the year ended December 31, 2007 and the quarter ended September 30, 2007 will be presented in future filings.

|   | PTGI                                      | PTHI       | Other    | PTGI                                    | PTHI       | Other     |
|---|---|------------|----------|---|------------|-----------|
|   | For the six months ended<br>June 30, 2007 |            |          | For the year ended<br>December 31, 2007 |            |           |
| <b>Statements of Operations:</b>                    |   |            |          |   |            |           |
| Intercompany interest                               | \$ (1,633)                                | \$ (2,782) | \$ 4,415 | \$ (4,037)                              | \$ (7,881) | \$ 11,918 |
| Equity in net income (loss) of subsidiaries         | \$ 1,633                                  | \$ 4,415   | \$       | \$ 4,037                                | \$ 11,918  | \$        |
| Net income  | \$  | \$ 1,633   | \$ 4,415 | \$                                      | \$ 4,037   | \$ 11,918 |
| <b>Statements of Cash Flows:</b>                    |   |            |          |   |            |           |
| Net cash used in operating activities               | \$ (1,633)                                | \$ (2,782) | \$ 4,415 | \$ (4,037)                              | \$ (7,881) | \$ 11,918 |
| Net cash provided by investing activities           | 1,633                                     | 2,782      |          | 4,037                                   | 7,881      |           |
| Net cash provided by (used in) financing activities |   |            | (4,415)  |   |            | (11,918)  |
| Net change in cash and cash equivalents             | \$  | \$         | \$       | \$                                      | \$         | \$        |

|                                      | December 31, 2007 |  |                               |
|--------------------------------------|-------------------|--|-------------------------------|
| <b>Balance sheets:</b>               |                   |  |                               |
| Investment in subsidiaries           |                   |  | \$ 4,037 \$ 11,918 \$         |
| Intercompany payable                 |                   |  | \$ 4,037 \$ 7,881 \$ (11,918) |
| Total stockholders' equity (deficit) |                   |  | \$ 4,037 \$ 11,918 \$         |

|   | PTGI                                      | IHC      | Guarantor<br>Subsidiaries | PTGI                                    | IHC       | Guarantor<br>Subsidiaries |
|---|---|----------|---------------------------|---|-----------|---------------------------|
|   | For the six months ended<br>June 30, 2007 |          |                           | For the year ended<br>December 31, 2007 |           |                           |
| <b>Statements of Operations:</b>                    |   |          |                           |   |           |                           |
| Intercompany interest                               | \$ (1,633)                                | \$ 4,415 | \$ (2,782)                | \$ (4,037)                              | \$ 11,918 | \$ (7,881)                |
| Equity in net income (loss) of subsidiaries         | \$ 1,633                                  | \$       | \$ 4,415                  | \$ 4,037                                | \$        | \$ 11,918                 |
| Net income  | \$  | \$ 4,415 | \$ 1,633                  | \$                                      | \$ 11,918 | \$ 4,037                  |
| <b>Statements of Cash Flows:</b>                    |   |          |                           |   |           |                           |
| Net cash used in operating activities               | \$ (1,633)                                | \$ 4,415 | \$ (2,782)                | \$ (4,037)                              | \$ 11,918 | \$ (7,881)                |
| Net cash provided by investing activities           | 1,633                                     |          | 2,782                     | 4,037                                   |           | 7,881                     |
| Net cash provided by (used in) financing activities |   | (4,415)  |                           |   | (11,918)  |                           |
| Net change in cash and cash equivalents             | \$  | \$       | \$                        | \$                                      | \$        | \$                        |

|                            | December 31, 2007 |  |                       |
|----------------------------|-------------------|--|-----------------------|
| <b>Balance sheets:</b>     |                   |  |                       |
| Intercompany receivable    |                   |  | \$ 11,918 \$          |
| Investment in subsidiaries |                   |  | \$ 4,037 \$ 11,918 \$ |

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|                                      |          |           |          |
|--------------------------------------|----------|-----------|----------|
| Intercompany payable                 | \$ 4,037 | \$        | \$ 7,881 |
| Total stockholders' equity (deficit) | \$       | \$ 11,918 | \$ 4,037 |

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In each consolidating presentation, the above described changes are completely offset by corresponding increases in the elimination entries. Accordingly, these changes have no effect on the Company's consolidated financial statements.

The consolidating condensed statement of cash flows for the six months ended June 30, 2007 has been restated to correct the presentation of transactions that are settled, on a net basis, through the Company's intercompany payables and receivables between PTGI (parent) and its subsidiaries and between PTHI and its subsidiaries. The Company had previously presented all such transactions as operating activities. Certain of these transactions should have been presented as investing and financing activities. Accordingly, the previous presentation of the statements of cash flows for the six months ended June 30, 2007 as contained in this Note have been corrected to add the lines entitled Proceeds from intercompany balance to cash flows from investing activities and Proceeds from (payments on) intercompany balance to cash flows from financing activities. In each consolidating presentation, the above described changes are completely offset by corresponding increases in the elimination entries. Accordingly, these changes have no effect on the Company's consolidated financial statements.

**Consolidating Financial Statements for PTHI Debt Issuances**

PTHI's 8% Senior Notes and 5% Exchangeable Senior Notes are fully and unconditionally guaranteed by PTGI on a senior basis as of June 30, 2008. PTGI has a 100% ownership in PTHI and no direct subsidiaries other than PTHI. Accordingly, the following consolidating condensed financial information as of June 30, 2008 and December 31, 2007 and for three months and six months ended June 30, 2008 and June 30, 2007 are included for (a) PTGI on a stand-alone basis; (b) PTHI on a stand-alone basis; (c) PTGI's indirect non-guarantor subsidiaries on a combined basis; and (d) PTGI on a consolidated basis.

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**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**  
**CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS**

(in thousands)

|  | For the Three Months Ended June 30, 2008 |           |            |              |              |
|--|--|-----------|------------|--------------|--------------|
|  | PTGI                                     | PTHI      | Other      | Eliminations | Consolidated |
|  | \$                                       | \$        | \$         | \$           | \$           |
| NET REVENUE  |  |           | \$ 236,462 |              | \$ 236,462   |
| OPERATING EXPENSES   |  |           |            |              |              |
| Cost of revenue (exclusive of depreciation included below)             |  |           | 142,739    |              | 142,739      |
| Selling, general and administrative                                    | 1,302                                    | 1,881     | 67,064     |              | 70,247       |
| Depreciation and amortization  |  |           | 8,095      |              | 8,095        |
| Loss on sale or disposal of assets                                     |  |           | 115        |              | 115          |
| Total operating expenses   | 1,302                                    | 1,881     | 218,013    |              | 221,196      |
| INCOME (LOSS) FROM OPERATIONS  | (1,302)                                  | (1,881)   | 18,449     |              | 15,266       |
| INTEREST EXPENSE   | (1,391)                                  | (6,891)   | (5,272)    |              | (13,554)     |
| ACCRETION ON DEBT PREMIUM (DISCOUNT)                                   | (137)                                    |           | 354        |              | 217          |
| GAIN (LOSS) ON EARLY EXTINGUISHMENT OR<br>RESTRUCTURING OF DEBT        | 9,861                                    | 22,784    | (468)      |              | 32,177       |
| INTEREST AND OTHER INCOME  | 5  |           | 1,987      |              | 1,992        |
| FOREIGN CURRENCY TRANSACTION GAIN                                      | 1,399                                    | 103       | 6,632      |              | 8,134        |
| INTERCOMPANY INTEREST  | (4,815)                                  | 210       | 4,605      |              |              |
| MANAGEMENT FEE   |  | 1,048     | (1,048)    |              |              |
| INCOME BEFORE INCOME TAXES AND EQUITY IN NET<br>INCOME OF SUBSIDIARIES | 3,620                                    | 15,373    | 25,239     |              | 44,232       |
| INCOME TAX BENEFIT   | 294                                      | 1,558     | 531        |              | 2,383        |
| INCOME BEFORE EQUITY IN NET INCOME OF<br>SUBSIDIARIES                  | 3,914                                    | 16,931    | 25,770     |              | 46,615       |
| EQUITY IN NET INCOME OF SUBSIDIARIES                                   | 42,610                                   | 25,679    |            | (68,289)     |              |
| INCOME FROM CONTINUING OPERATIONS                                      | 46,524                                   | 42,610    | 25,770     | (68,289)     | 46,615       |
| LOSS FROM DISCONTINUED OPERATIONS, net of tax                          |  |           | (91)       |              | (91)         |
| NET INCOME   | \$ 46,524                                | \$ 42,610 | \$ 25,679  | \$ (68,289)  | \$ 46,524    |



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**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**  
**CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS**

(in thousands)

|  | For the Six Months Ended June 30, 2008 |           |            |              |              |
|--|--|-----------|------------|--------------|--------------|
|  | PTGI                                   | PTHI      | Other      | Eliminations | Consolidated |
| NET REVENUE  | \$                                     | \$        | \$ 462,542 | \$           | \$ 462,542   |
| OPERATING EXPENSES   |  |           |            |              |              |
| Cost of revenue (exclusive of depreciation included below)             |  |           | 284,518    |              | 284,518      |
| Selling, general and administrative                                    | 2,574                                  | 3,609     | 133,233    |              | 139,416      |
| Depreciation and amortization  |  |           | 16,056     |              | 16,056       |
| Gain on sale or disposal of assets                                     |  |           | (2,465)    |              | (2,465)      |
| Total operating expenses   | 2,574                                  | 3,609     | 431,342    |              | 437,525      |
| INCOME (LOSS) FROM OPERATIONS  | (2,574)                                | (3,609)   | 31,200     |              | 25,017       |
| INTEREST EXPENSE   | (3,308)                                | (14,801)  | (10,638)   |              | (28,747)     |
| ACCRETION ON DEBT PREMIUM (DISCOUNT)                                   | (512)                                  |           | 699        |              | 187          |
| GAIN (LOSS) ON EARLY EXTINGUISHMENT OR<br>RESTRUCTURING OF DEBT        | 12,070                                 | 22,784    | (367)      |              | 34,487       |
| INTEREST AND OTHER INCOME  | 15                                     |           | 2,942      |              | 2,957        |
| FOREIGN CURRENCY TRANSACTION GAIN                                      | 2,695                                  | 472       | 6,674      |              | 9,841        |
| INTERCOMPANY INTEREST  | (5,162)                                | (3,183)   | 8,345      |              |              |
| MANAGEMENT FEE   |  | 2,991     | (2,991)    |              |              |
| INCOME BEFORE INCOME TAXES AND EQUITY IN<br>NET INCOME OF SUBSIDIARIES | 3,224                                  | 4,654     | 35,864     |              | 43,742       |
| INCOME TAX BENEFIT (EXPENSE)   | 210                                    | 1,087     | (1,334)    |              | (37)         |
| INCOME BEFORE EQUITY IN NET INCOME OF<br>SUBSIDIARIES                  | 3,434                                  | 5,741     | 34,530     |              | 43,705       |
| EQUITY IN NET INCOME OF SUBSIDIARIES                                   | 40,091                                 | 34,350    |            | (74,441)     |              |
| INCOME FROM CONTINUING OPERATIONS                                      | 43,525                                 | 40,091    | 34,530     | (74,441)     | 43,705       |
| LOSS FROM DISCONTINUED OPERATIONS, net of tax                          |  |           | (180)      |              | (180)        |
| NET INCOME   | \$ 43,525                              | \$ 40,091 | \$ 34,350  | \$ (74,441)  | \$ 43,525    |

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**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**  
**CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS**

(in thousands)

|   | For the Three Months Ended June 30, 2007 |           |            |              |              |
|---|--|-----------|------------|--------------|--------------|
|   | PTGI                                     | PTHI      | Other      | Eliminations | Consolidated |
| NET REVENUE   | \$                                       | \$        | \$ 226,430 | \$           | \$ 226,430   |
| OPERATING EXPENSES  |  |           |            |              |              |
| Cost of revenue (exclusive of depreciation included below)                    |  |           | 141,643    |              | 141,643      |
| Selling, general and administrative   | 1,242                                    | 2,939     | 64,335     |              | 68,516       |
| Depreciation and amortization   |  |           | 7,343      |              | 7,343        |
| Loss on sale or disposal of assets  |  |           | 676        |              | 676          |
| Total operating expenses  | 1,242                                    | 2,939     | 213,997    |              | 218,178      |
| INCOME (LOSS) FROM OPERATIONS   | (1,242)                                  | (2,939)   | 12,433     |              | 8,252        |
| INTEREST EXPENSE  | (2,406)                                  | (7,987)   | (6,031)    |              | (16,424)     |
| ACCRETION ON DEBT PREMIUM (DISCOUNT)  | (391)                                    |           | 315        |              | (76)         |
| LOSS ON EARLY EXTINGUISHMENT OR<br>RESTRUCTURING OF DEBT                      | (2,311)                                  | (4)       |            |              | (2,315)      |
| INTEREST AND OTHER INCOME   | 48                                       |           | 1,010      |              | 1,058        |
| FOREIGN CURRENCY TRANSACTION GAIN (LOSS)                                      | (2,103)                                  | 2,877     | 14,307     |              | 15,081       |
| INTERCOMPANY INTEREST   | (1,125)                                  | (4,923)   | 6,048      |              |              |
| MANAGEMENT FEE  |  | 1,244     | (1,244)    |              |              |
| INCOME (LOSS) BEFORE INCOME TAXES AND EQUITY<br>IN NET INCOME OF SUBSIDIARIES | (9,530)                                  | (11,732)  | 26,838     |              | 5,576        |
| INCOME TAX BENEFIT (EXPENSE)  | 2,397                                    | (221)     | 4,515      |              | 6,691        |
| INCOME (LOSS) BEFORE EQUITY IN NET INCOME OF<br>SUBSIDIARIES                  | (7,133)                                  | (11,953)  | 31,353     |              | 12,267       |
| EQUITY IN NET INCOME OF SUBSIDIARIES  | 19,234                                   | 31,187    |            | (50,421)     |              |
| INCOME FROM CONTINUING OPERATIONS   | 12,101                                   | 19,234    | 31,353     | (50,421)     | 12,267       |
| LOSS FROM DISCONTINUED OPERATIONS, net of tax                                 |  |           | (166)      |              | (166)        |
| NET INCOME  | \$ 12,101                                | \$ 19,234 | \$ 31,187  | \$ (50,421)  | \$ 12,101    |

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**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**  
**CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS**

(in thousands)

|   | For the Six Months Ended June 30, 2007 |           |            |              |              |
|---|--|-----------|------------|--------------|--------------|
|   | PTGI                                   | PTHI      | Other      | Eliminations | Consolidated |
| NET REVENUE   | \$                                     | \$        | \$ 452,433 | \$           | \$ 452,433   |
| OPERATING EXPENSES  |  |           |            |              |              |
| Cost of revenue (exclusive of depreciation included below)                    |  |           | 285,659    |              | 285,659      |
| Selling, general and administrative   | 2,498                                  | 6,656     | 127,058    |              | 136,212      |
| Depreciation and amortization   |  |           | 13,900     |              | 13,900       |
| Loss on sale or disposal of assets  |  |           | 684        |              | 684          |
| Total operating expenses  | 2,498                                  | 6,656     | 427,301    |              | 436,455      |
| INCOME (LOSS) FROM OPERATIONS   | (2,498)                                | (6,656)   | 25,132     |              | 15,978       |
| INTEREST EXPENSE  | (5,803)                                | (15,799)  | (8,256)    |              | (29,858)     |
| ACCRETION ON DEBT PREMIUM (DISCOUNT)  | (791)                                  |           | 417        |              | (374)        |
| LOSS ON EARLY EXTINGUISHMENT OR<br>RESTRUCTURING OF DEBT                      | (2,311)                                | (4)       | (5,959)    |              | (8,274)      |
| INTEREST AND OTHER INCOME   | 334                                    |           | 2,220      |              | 2,554        |
| FOREIGN CURRENCY TRANSACTION GAIN   | 3,848                                  | 455       | 13,752     |              | 18,055       |
| INTERCOMPANY INTEREST   | (673)                                  | (5,184)   | 5,857      |              |              |
| MANAGEMENT FEE  |  | 3,257     | (3,257)    |              |              |
| INCOME (LOSS) BEFORE INCOME TAXES AND EQUITY<br>IN NET INCOME OF SUBSIDIARIES | (7,894)                                | (23,931)  | 29,906     |              | (1,919)      |
| INCOME TAX BENEFIT (EXPENSE)  | 2,472                                  | (221)     | 3,435      |              | 5,686        |
| INCOME (LOSS) BEFORE EQUITY IN NET INCOME OF<br>SUBSIDIARIES                  | (5,422)                                | (24,152)  | 33,341     |              | 3,767        |
| EQUITY IN NET INCOME OF SUBSIDIARIES  | 14,881                                 | 39,033    |            | (53,914)     |              |
| INCOME FROM CONTINUING OPERATIONS   | 9,459                                  | 14,881    | 33,341     | (53,914)     | 3,767        |
| LOSS FROM DISCONTINUED OPERATIONS, net of tax                                 |  |           | (266)      |              | (266)        |
| GAIN FROM SALE OF DISCONTINUED OPERATIONS,<br>net of tax                      |  |           | 5,958      |              | 5,958        |
| NET INCOME  | \$ 9,459                               | \$ 14,881 | \$ 39,033  | \$ (53,914)  | \$ 9,459     |

**Table of Contents****PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED****CONSOLIDATING CONDENSED BALANCE SHEET**

(in thousands)

|  | PTGI              | PTHI              | June 30, 2008<br>Other | Eliminations        | Consolidated      |
|--|-------------------|-------------------|------------------------|---------------------|-------------------|
| <b>ASSETS</b>  |                   |                   |                        |                     |                   |
| <b>CURRENT ASSETS:</b>                               |                   |                   |                        |                     |                   |
| Cash and cash equivalents                            | \$ 4,810          | \$ (73)           | \$ 50,813              | \$                  | \$ 55,550         |
| Restricted cash                                      |                   |                   |                        |                     |                   |
| Accounts receivable                                  |                   |                   | 118,412                |                     | 118,412           |
| Prepaid expenses and other current assets            | 123               | 4                 | 19,343                 |                     | 19,470            |
| <b>Total current assets</b>                          | <b>4,933</b>      | <b>(69)</b>       | <b>188,568</b>         |                     | <b>193,432</b>    |
| INTERCOMPANY RECEIVABLES                             | 96,854            | 1,071,411         |                        | (1,168,265)         |                   |
| INVESTMENTS IN SUBSIDIARIES                          | 41,447            | (619,846)         |                        | 578,399             |                   |
| RESTRICTED CASH                                      |                   |                   | 10,782                 |                     | 10,782            |
| PROPERTY AND EQUIPMENT Net                           |                   |                   | 147,753                |                     | 147,753           |
| GOODWILL   |                   |                   | 40,539                 |                     | 40,539            |
| OTHER INTANGIBLE ASSETS Net                          |                   |                   | 989                    |                     | 989               |
| OTHER ASSETS   | 527               | 5,163             | 27,741                 |                     | 33,431            |
| <b>TOTAL ASSETS</b>                                  | <b>\$ 143,761</b> | <b>\$ 456,659</b> | <b>\$ 416,372</b>      | <b>\$ (589,866)</b> | <b>\$ 426,926</b> |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY (DEFICIT)</b> |                   |                   |                        |                     |                   |
| <b>CURRENT LIABILITIES:</b>                          |                   |                   |                        |                     |                   |
| Accounts payable                                     | \$ 359            | \$ 168            | 59,807                 | \$                  | \$ 60,334         |
| Accrued interconnection costs                        |                   |                   | 49,396                 |                     | 49,396            |
| Deferred revenue                                     |                   |                   | 15,839                 |                     | 15,839            |
| Accrued expenses and other current liabilities       | 274               | 997               | 52,247                 |                     | 53,518            |
| Accrued income taxes                                 | 85                |                   | 26,237                 |                     | 26,322            |
| Accrued interest                                     | 1,173             | 8,468             | 1,550                  |                     | 11,191            |
| Current portion of long-term obligations             |                   | 2,168             | 7,133                  |                     | 9,301             |
| <b>Total current liabilities</b>                     | <b>1,891</b>      | <b>11,801</b>     | <b>212,209</b>         |                     | <b>225,901</b>    |
| INTERCOMPANY PAYABLES                                | 493,361           | 97,123            | 577,781                | (1,168,265)         |                   |
| LONG-TERM OBLIGATIONS (net of premium of \$4,452)    | 56,440            | 306,288           | 246,148                |                     | 608,876           |
| OTHER LIABILITIES                                    |                   |                   | 80                     |                     | 80                |
| <b>Total liabilities</b>                             | <b>551,692</b>    | <b>415,212</b>    | <b>1,036,218</b>       | <b>(1,168,265)</b>  | <b>834,857</b>    |
| <b>COMMITMENTS AND CONTINGENCIES</b>                 |                   |                   |                        |                     |                   |
| <b>STOCKHOLDERS EQUITY (DEFICIT):</b>                |                   |                   |                        |                     |                   |
| Common stock   | 1,426             |                   |                        |                     | 1,426             |
| Additional paid-in capital                           | 718,827           | 1,161,930         | 305,844                | (1,467,774)         | 718,827           |
| Accumulated deficit                                  | (1,031,253)       | (1,024,352)       | (838,264)              | 1,862,616           | (1,031,253)       |
| Accumulated other comprehensive loss                 | (96,931)          | (96,131)          | (87,426)               | 183,557             | (96,931)          |
| <b>Total stockholders equity (deficit)</b>           | <b>(407,931)</b>  | <b>41,447</b>     | <b>(619,846)</b>       | <b>578,399</b>      | <b>(407,931)</b>  |

|  |            |            |            |              |            |
|--|------------|------------|------------|--------------|------------|
| TOTAL LIABILITIES AND STOCKHOLDERS<br>EQUITY (DEFICIT) | \$ 143,761 | \$ 456,659 | \$ 416,372 | \$ (589,866) | \$ 426,926 |
|--|------------|------------|------------|--------------|------------|

**Table of Contents****PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED****CONSOLIDATING CONDENSED BALANCE SHEET**

(in thousands)

|  | PTGI             | PTHI              | December 31, 2007 |                     | Consolidated      |
|--|------------------|-------------------|-------------------|---------------------|-------------------|
|  |                  |                   | Other             | Eliminations        |                   |
| <b>ASSETS</b>  |                  |                   |                   |                     |                   |
| <b>CURRENT ASSETS:</b>                               |                  |                   |                   |                     |                   |
| Cash and cash equivalents                            | \$ 1,299         | \$ (35)           | \$ 80,018         | \$                  | \$ 81,282         |
| Restricted cash                                      |                  |                   | 362               |                     | 362               |
| Accounts receivable                                  |                  |                   | 113,588           |                     | 113,588           |
| Prepaid expenses and other current assets            | 308              |                   | 28,352            |                     | 28,660            |
| <b>Total current assets</b>                          | <b>1,607</b>     | <b>(35)</b>       | <b>222,320</b>    |                     | <b>223,892</b>    |
| INTERCOMPANY RECEIVABLES                             | 88,536           | 1,089,076         |                   | (1,177,612)         |                   |
| INVESTMENTS IN SUBSIDIARIES                          | 5,404            | (650,148)         |                   | 644,744             |                   |
| RESTRICTED CASH                                      |                  |                   | 9,677             |                     | 9,677             |
| PROPERTY AND EQUIPMENT Net                           |                  |                   | 144,599           |                     | 144,599           |
| GOODWILL   |                  |                   | 40,134            |                     | 40,134            |
| OTHER INTANGIBLE ASSETS Net                          |                  |                   | 1,557             |                     | 1,557             |
| OTHER ASSETS   | 2,389            | 7,095             | 31,060            |                     | 40,544            |
| <b>TOTAL ASSETS</b>                                  | <b>\$ 97,936</b> | <b>\$ 445,988</b> | <b>\$ 449,347</b> | <b>\$ (532,868)</b> | <b>\$ 460,403</b> |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY (DEFICIT)</b> |                  |                   |                   |                     |                   |
| <b>CURRENT LIABILITIES:</b>                          |                  |                   |                   |                     |                   |
| Accounts payable                                     | \$ 805           | \$ 407            | 73,681            | \$                  | \$ 74,893         |
| Accrued interconnection costs                        |                  |                   | 44,911            |                     | 44,911            |
| Deferred revenue                                     |                  |                   | 16,513            |                     | 16,513            |
| Accrued expenses and other current liabilities       | 207              | 1,225             | 52,988            |                     | 54,420            |
| Accrued income taxes                                 | 306              | 1,522             | 28,963            |                     | 30,791            |
| Accrued interest                                     | 2,388            | 8,701             | 1,371             |                     | 12,460            |
| Current portion of long-term obligations             |                  | 3,816             | 7,412             |                     | 11,228            |
| <b>Total current liabilities</b>                     | <b>3,706</b>     | <b>15,671</b>     | <b>225,839</b>    |                     | <b>245,216</b>    |
| INTERCOMPANY PAYABLES                                | 424,978          | 33,116            | 719,518           | (1,177,612)         |                   |
| LONG-TERM OBLIGATIONS (net of premium of \$2,528)    | 116,792          | 391,797           | 154,086           |                     | 662,675           |
| OTHER LIABILITIES                                    |                  |                   | 52                |                     | 52                |
| <b>Total liabilities</b>                             | <b>545,476</b>   | <b>440,584</b>    | <b>1,099,495</b>  | <b>(1,177,612)</b>  | <b>907,943</b>    |
| <b>COMMITMENTS AND CONTINGENCIES</b>                 |                  |                   |                   |                     |                   |
| <b>STOCKHOLDERS EQUITY (DEFICIT):</b>                |                  |                   |                   |                     |                   |
| Common stock   | 1,426            |                   |                   |                     | 1,426             |
| Additional paid-in capital                           | 718,695          | 1,161,930         | 305,844           | (1,467,774)         | 718,695           |
| Accumulated deficit                                  | (1,074,778)      | (1,064,443)       | (872,614)         | 1,937,057           | (1,074,778)       |
| Accumulated other comprehensive loss                 | (92,883)         | (92,083)          | (83,378)          | 175,461             | (92,883)          |
| <b>Total stockholders equity (deficit)</b>           | <b>(447,540)</b> | <b>5,404</b>      | <b>(650,148)</b>  | <b>644,744</b>      | <b>(447,540)</b>  |

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|  |           |            |            |              |            |
|--|-----------|------------|------------|--------------|------------|
| TOTAL LIABILITIES AND STOCKHOLDERS<br>EQUITY (DEFICIT) | \$ 97,936 | \$ 445,988 | \$ 449,347 | \$ (532,868) | \$ 460,403 |
|--|-----------|------------|------------|--------------|------------|

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**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**  
**CONSOLIDATING CONDENSED STATEMENT OF CASH FLOWS**

(in thousands)

|   | For Six Months Ended June 30, 2008 |           |           |              |              |
|---|------------------------------------|-----------|-----------|--------------|--------------|
|   | PTGI                               | PTHI      | Other     | Eliminations | Consolidated |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>  |                                    |           |           |              |              |
| Net income  | \$ 43,525                          | \$ 40,091 | \$ 34,350 | \$ (74,441)  | \$ 43,525    |
| Adjustments to reconcile net income to net cash provided by operating activities:                                 |                                    |           |           |              |              |
| Provision for doubtful accounts receivable  |                                    |           | 5,696     |              | 5,696        |
| Stock compensation expense  |                                    | 132       |           |              | 132          |
| Depreciation and amortization   |                                    |           | 16,056    |              | 16,056       |
| Gain on sale or disposal of assets  |                                    |           | (2,465)   |              | (2,465)      |
| Accretion of debt (premium) discount  | 512                                |           | (699)     |              | (187)        |
| Equity in net income of subsidiary  | (40,091)                           | (34,350)  |           | 74,441       |              |
| Deferred income taxes   |                                    | 450       | 2,395     |              | 2,845        |
| Gain (loss) on early extinguishment or restructuring of debt  | (12,070)                           | (22,784)  | 367       |              | (34,487)     |
| Unrealized foreign currency transaction gain on intercompany and foreign debt                                     | (2,684)                            | (487)     | (6,457)   |              | (9,628)      |
| Changes in assets and liabilities, net of acquisitions:   |                                    |           |           |              |              |
| Increase in accounts receivable   |                                    |           | (6,388)   |              | (6,388)      |
| (Increase) decrease in prepaid expenses and other current assets  | 185                                | (4)       | 11,053    |              | 11,234       |
| (Increase) decrease in other assets   | 388                                | 579       | (62)      |              | 905          |
| Decrease in accounts payable  | (447)                              | (239)     | (15,953)  |              | (16,639)     |
| Increase in accrued interconnection costs   |                                    |           | 3,159     |              | 3,159        |
| Increase (decrease), net, in deferred revenue, accrued expenses, other current liabilities, and other liabilities | 67                                 | (235)     | (2,911)   |              | (3,079)      |
| Decrease in accrued income taxes  | (222)                              | (1,522)   | (2,711)   |              | (4,455)      |
| Increase (decrease) in accrued interest   | (871)                              | (223)     | 173       |              | (921)        |
| Net cash provided by (used in) operating activities   | (11,708)                           | (18,592)  | 35,603    |              | 5,303        |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>  |                                    |           |           |              |              |
| Purchase of property and equipment  |                                    |           | (14,599)  |              | (14,599)     |
| Sale of property and equipment  |                                    |           | 805       |              | 805          |
| Cash from disposition of business, net of cash disposed   |                                    |           | 1,676     |              | 1,676        |
| Cash used in business acquisitions, net of cash acquired  |                                    |           | (34)      |              | (34)         |
| Decrease in restricted cash   |                                    |           | 103       |              | 103          |
| Proceeds from intercompany balance  | 27,636                             | 17,339    |           | (44,975)     |              |
| Net cash provided by (used in) investing activities   | 27,636                             | 17,339    | (12,049)  | (44,975)     | (12,049)     |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>  |                                    |           |           |              |              |
| Purchase of the Company's debt securities   | (11,217)                           |           |           |              | (11,217)     |
| Principal payments on long-term obligations   | (1,200)                            | (5,232)   | (1,855)   |              | (8,287)      |
| Proceeds from (payments on) intercompany balance  |                                    | 6,447     | (51,422)  | 44,975       |              |
| Net cash provided by (used in) financing activities   | (12,417)                           | 1,215     | (53,277)  | 44,975       | (19,504)     |
| <b>EFFECTS OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>  |                                    |           |           |              |              |
|   |                                    |           | 518       |              | 518          |



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|  |          |         |           |           |
|--|----------|---------|-----------|-----------|
| NET CHANGE IN CASH AND CASH EQUIVALENTS        | 3,511    | (38)    | (29,205)  | (25,732)  |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD | 1,299    | (35)    | 80,018    | 81,282    |
| CASH AND CASH EQUIVALENTS, END OF PERIOD       | \$ 4,810 | \$ (73) | \$ 50,813 | \$ 55,550 |

**Table of Contents****PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED****CONSOLIDATING CONDENSED STATEMENT OF CASH FLOWS**

(in thousands)

|  | For Six Months Ended June 30, 2007 |           |           |              |              |
|--|------------------------------------|-----------|-----------|--------------|--------------|
|  | PTGI                               | PTHI      | Other     | Eliminations | Consolidated |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>   |                                    |           |           |              |              |
| Net income   | \$ 9,459                           | \$ 14,881 | \$ 39,033 | \$ (53,914)  | \$ 9,459     |
| Adjustments to reconcile net income to net cash provided by operating activities:  |                                    |           |           |              |              |
| Provision for doubtful accounts receivable   |                                    |           | 4,885     |              | 4,885        |
| Stock compensation expense   |                                    | 125       |           |              | 125          |
| Depreciation and amortization  |                                    |           | 13,946    |              | 13,946       |
| Gain on sale or disposal of assets   |                                    |           | (5,078)   |              | (5,078)      |
| Accretion of debt (premium) discount   | 791                                |           | (417)     |              | 374          |
| Equity in net income of subsidiary   | (14,881)                           | (39,033)  |           | 53,914       |              |
| Loss on early extinguishment or restructuring of debt  | 2,311                              | 4         | 5,959     |              | 8,274        |
| Unrealized foreign currency transaction gain on intercompany and foreign debt  | (7,550)                            | (2,194)   | (9,763)   |              | (19,507)     |
| Changes in assets and liabilities, net of acquisitions:  |                                    |           |           |              |              |
| Decrease in accounts receivable  |                                    |           | 1,028     |              | 1,028        |
| Decrease in prepaid expenses and other current assets  | 93                                 |           | 1,960     |              | 2,053        |
| (Increase) decrease in other assets  | 460                                | 488       | (1,054)   |              | (106)        |
| Increase (decrease) in accounts payable  | (287)                              | 3         | (272)     |              | (556)        |
| Decrease in accrued interconnection costs  |                                    |           | (4,645)   |              | (4,645)      |
| Increase (decrease), net, in deferred revenue, accrued expenses, other current liabilities, accrued income taxes and other liabilities | (3,242)                            | 1,081     | (1,754)   |              | (3,915)      |
| Increase (decrease) in accrued interest  | (1,581)                            | (97)      | 649       |              | (1,029)      |
| Net cash provided by (used in) operating activities  | (14,427)                           | (24,742)  | 44,477    |              | 5,308        |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>   |                                    |           |           |              |              |
| Purchase of property and equipment   |                                    |           | (17,041)  |              | (17,041)     |
| Cash from disposition of business, net of cash disposed  |                                    |           | 5,527     |              | 5,527        |
| Decrease in restricted cash  |                                    |           | 596       |              | 596          |
| Proceeds from intercompany balance   | 69,530                             | 40,325    |           | (109,855)    |              |
| Net cash provided by (used in) investing activities  | 69,530                             | 40,325    | (10,918)  | (109,855)    | (10,918)     |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>   |                                    |           |           |              |              |
| Proceeds from issuance of long-term obligations  |                                    |           | 109,275   |              | 109,275      |
| Deferred financing costs   |                                    |           | (6,570)   |              | (6,570)      |
| Principal payments on long-term obligations  | (54,882)                           | (479)     | (2,818)   |              | (58,179)     |
| Payment on intercompany balance  |                                    | (15,097)  | (94,758)  | 109,855      |              |
| Net cash provided by (used in) financing activities  | (54,882)                           | (15,576)  | 5,129     | 109,855      | 44,526       |
| <b>EFFECTS OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>   |                                    |           |           |              |              |
|  |                                    |           | 1,451     |              | 1,451        |
| NET CHANGE IN CASH AND CASH EQUIVALENTS  | 221                                | 7         | 40,139    |              | 40,367       |
| CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD   | 3,764                              | (28)      | 60,581    |              | 64,317       |

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|  |          |         |            |    |            |
|--|----------|---------|------------|----|------------|
| CASH AND CASH EQUIVALENTS, END OF PERIOD | \$ 3,985 | \$ (21) | \$ 100,720 | \$ | \$ 104,684 |
|--|----------|---------|------------|----|------------|

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**Consolidating Financial Statements for IHC Debt Issuance**

Primus Telecommunications IHC, Inc.'s 14/4% Senior Secured Notes are fully, unconditionally, jointly and severally guaranteed by PTGI on a senior basis as of June 30, 2008 and by PTHI, Primus Telecommunications, Inc., TresCom International Inc., Least Cost Routing, Inc., TresCom U.S.A., Inc., iPRIMUS USA, Inc., and iPRIMUS.com, Inc., 100% owned subsidiaries of PTGI (collectively, the "Other Guarantors"). PTGI has a 100% ownership in PTHI and no direct subsidiaries other than PTHI. Accordingly, the following consolidating condensed financial information as of June 30, 2008 and December 31, 2007 and for three months and six months ended June 30, 2008 and June 30, 2007 are included for (a) PTGI on a stand-alone basis; (b) Primus Telecommunications IHC, Inc. (IHC) on a stand-alone basis; (c) the Other Guarantor subsidiaries on a combined basis; (d) PTGI's indirect non-guarantor subsidiaries on a combined basis and (e) PTGI on a consolidated basis.

Investments in subsidiaries are accounted for using the equity method for purposes of the consolidating presentation. The principal elimination entries eliminate investments in subsidiaries, intercompany balances and intercompany transactions.

**Table of Contents****PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED****CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS**

(in thousands)

|   | For Three Months Ended June 30, 2008 |          |                           |                               |              | Consolidated |
|---|--------------------------------------|----------|---------------------------|-------------------------------|--------------|--------------|
|   | PTGI                                 | IHC      | Guarantor<br>Subsidiaries | Non Guarantor<br>Subsidiaries | Eliminations |              |
| NET REVENUE   | \$                                   | \$       | \$ 34,664                 | \$ 201,798                    | \$           | \$ 236,462   |
| OPERATING EXPENSES  |                                      |          |                           |                               |              |              |
| Cost of revenue (exclusive of depreciation included below)          |                                      |          | 28,027                    | 114,712                       |              | 142,739      |
| Selling, general and administrative                                 | 1,302                                | 83       | 9,230                     | 59,632                        |              | 70,247       |
| Depreciation and amortization                                       |                                      |          | 815                       | 7,280                         |              | 8,095        |
| (Gain) loss on sale or disposal of assets                           |                                      |          | (5)                       | 120                           |              | 115          |
| Total operating expenses  | 1,302                                | 83       | 38,067                    | 181,744                       |              | 221,196      |
| INCOME (LOSS) FROM OPERATIONS                                       | (1,302)                              | (83)     | (3,403)                   | 20,054                        |              | 15,266       |
| INTEREST EXPENSE  | (1,391)                              | (3,932)  | (6,894)                   | (1,337)                       |              | (13,554)     |
| ACCRETION ON DEBT PREMIUM (DISCOUNT)                                | (137)                                | 354      |                           |                               |              | 217          |
| INCOME (LOSS) ON EARLY EXTINGUISHMENT OR RESTRUCTURING OF DEBT      | 9,861                                | (468)    | 22,784                    |                               |              | 32,177       |
| INTEREST AND OTHER INCOME   | 5                                    |          | 2                         | 1,985                         |              | 1,992        |
| FOREIGN CURRENCY TRANSACTION GAIN                                   | 1,399                                | 2,762    | 116                       | 3,857                         |              | 8,134        |
| INTERCOMPANY INTEREST   | (4,815)                              | 169      | 210                       | 4,436                         |              |              |
| MANAGEMENT FEE  |                                      |          | 1,146                     | (1,146)                       |              |              |
| ROYALTY FEE   |                                      | 3,549    | 136                       | (3,685)                       |              |              |
| INCOME BEFORE INCOME TAXES AND EQUITY IN NET INCOME OF SUBSIDIARIES | 3,620                                | 2,351    | 14,097                    | 24,164                        |              | 44,232       |
| INCOME TAX BENEFIT  | 294                                  | 935      | 1,129                     | 25                            |              | 2,383        |
| INCOME BEFORE EQUITY IN NET INCOME OF SUBSIDIARIES                  | 3,914                                | 3,286    | 15,226                    | 24,189                        |              | 46,615       |
| EQUITY IN NET INCOME OF SUBSIDIARIES                                | 42,610                               |          | 25,679                    |                               | (68,289)     |              |
| INCOME FROM CONTINUING OPERATIONS                                   | 46,524                               | 3,286    | 40,905                    | 24,189                        | (68,289)     | 46,615       |
| LOSS FROM DISCONTINUED OPERATIONS, net of tax                       |                                      |          |                           |                               | (91)         | (91)         |
| NET INCOME  | \$ 46,524                            | \$ 3,286 | \$ 40,905                 | \$ 24,098                     | \$ (68,289)  | \$ 46,524    |

**Table of Contents****PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED****CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS**

(in thousands)

|   | For Six Months Ended June 30, 2008 |          |                           |                               |              | Consolidated |
|---|------------------------------------|----------|---------------------------|-------------------------------|--------------|--------------|
|   | PTGI                               | IHC      | Guarantor<br>Subsidiaries | Non Guarantor<br>Subsidiaries | Eliminations |              |
| NET REVENUE   | \$                                 | \$       | \$ 69,697                 | \$ 392,845                    | \$           | \$ 462,542   |
| OPERATING EXPENSES  |                                    |          |                           |                               |              |              |
| Cost of revenue (exclusive of depreciation included below)          |                                    |          | 55,590                    | 228,928                       |              | 284,518      |
| Selling, general and administrative                                 | 2,574                              | 118      | 18,076                    | 118,648                       |              | 139,416      |
| Depreciation and amortization                                       |                                    |          | 1,681                     | 14,375                        |              | 16,056       |
| Loss on sale or disposal of assets                                  |                                    |          | (805)                     | (1,660)                       |              | (2,465)      |
| Total operating expenses  | 2,574                              | 118      | 74,542                    | 360,291                       |              | 437,525      |
| INCOME (LOSS) FROM OPERATIONS                                       | (2,574)                            | (118)    | (4,845)                   | 32,554                        |              | 25,017       |
| INTEREST EXPENSE  | (3,308)                            | (7,804)  | (14,972)                  | (2,663)                       |              | (28,747)     |
| ACCRETION ON DEBT PREMIUM (DISCOUNT)                                | (512)                              | 699      |                           |                               |              | 187          |
| INCOME (LOSS) ON EARLY EXTINGUISHMENT OR RESTRUCTURING OF DEBT      | 12,070                             | (475)    | 22,784                    | 108                           |              | 34,487       |
| INTEREST AND OTHER INCOME   | 15                                 |          | (5)                       | 2,947                         |              | 2,957        |
| FOREIGN CURRENCY TRANSACTION GAIN                                   | 2,695                              | 3,488    | 514                       | 3,144                         |              | 9,841        |
| INTERCOMPANY INTEREST   | (5,162)                            | 5,859    | (3,183)                   | 2,486                         |              |              |
| MANAGEMENT FEE  |                                    |          | 3,251                     | (3,251)                       |              |              |
| ROYALTY FEE   |                                    | 7,306    |                           | (7,306)                       |              |              |
| INCOME BEFORE INCOME TAXES AND EQUITY IN NET INCOME OF SUBSIDIARIES | 3,224                              | 8,955    | 3,544                     | 28,019                        |              | 43,742       |
| INCOME TAX BENEFIT (EXPENSE)  | 210                                | 470      | 625                       | (1,342)                       |              | (37)         |
| INCOME BEFORE EQUITY IN NET INCOME OF SUBSIDIARIES                  | 3,434                              | 9,425    | 4,169                     | 26,677                        |              | 43,705       |
| EQUITY IN NET INCOME OF SUBSIDIARIES                                | 40,091                             |          | 34,350                    |                               | (74,441)     |              |
| INCOME FROM CONTINUING OPERATIONS                                   | 43,525                             | 9,425    | 38,519                    | 26,677                        | (74,441)     | 43,705       |
| LOSS FROM DISCONTINUED OPERATIONS, net of tax                       |                                    |          |                           | (180)                         |              | (180)        |
| NET INCOME  | \$ 43,525                          | \$ 9,425 | \$ 38,519                 | \$ 26,497                     | \$ (74,441)  | \$ 43,525    |

**Table of Contents**

**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**  
**CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS**

(in thousands)

|  | For the Three Months Ended June 30, 2007 |          |                           |                               |              | Consolidated |
|--|--|----------|---------------------------|-------------------------------|--------------|--------------|
|  | PTGI                                     | IHC      | Guarantor<br>Subsidiaries | Non Guarantor<br>Subsidiaries | Eliminations |              |
| NET REVENUE  | \$                                       | \$       | \$ 35,232                 | \$ 191,198                    | \$           | \$ 226,430   |
| OPERATING EXPENSES   |  |          |                           |                               |              |              |
| Cost of revenue (exclusive of depreciation included below)                 |  |          | 24,321                    | 117,322                       |              | 141,643      |
| Selling, general and administrative  | 1,242                                    | 21       | 11,704                    | 55,549                        |              | 68,516       |
| Depreciation and amortization  |  |          | 929                       | 6,414                         |              | 7,343        |
| Loss on sale or disposal of assets   |  |          |                           | 676                           |              | 676          |
| Total operating expenses   | 1,242                                    | 21       | 36,954                    | 179,961                       |              | 218,178      |
| INCOME (LOSS) FROM OPERATIONS  | (1,242)                                  | (21)     | (1,722)                   | 11,237                        |              | 8,252        |
| INTEREST EXPENSE   | (2,406)                                  | (3,556)  | (7,990)                   | (2,472)                       |              | (16,424)     |
| ACCRETION ON DEBT PREMIUM (DISCOUNT)                                       | (391)                                    |          |                           | 315                           |              | (76)         |
| LOSS ON EARLY EXTINGUISHMENT OR RESTRUCTURING OF DEBT                      | (2,311)                                  |          | (4)                       |                               |              | (2,315)      |
| INTEREST AND OTHER INCOME  | 48                                       |          | 12                        | 998                           |              | 1,058        |
| FOREIGN CURRENCY TRANSACTION GAIN (LOSS)                                   | (2,103)                                  | 3,728    | 2,902                     | 10,554                        |              | 15,081       |
| INTERCOMPANY INTEREST  | (1,125)                                  | 3,013    | (4,923)                   | 3,035                         |              |              |
| MANAGEMENT FEE   |  |          | 1,381                     | (1,381)                       |              |              |
| ROYALTY FEE  |  | 3,583    | (148)                     | (3,435)                       |              |              |
| INCOME (LOSS) BEFORE INCOME TAXES AND EQUITY IN NET INCOME OF SUBSIDIARIES | (9,530)                                  | 6,747    | (10,492)                  | 18,851                        |              | 5,576        |
| INCOME TAX BENEFIT (EXPENSE)   | 2,397                                    | (773)    | (315)                     | 5,382                         |              | 6,691        |
| INCOME (LOSS) BEFORE EQUITY IN NET INCOME OF SUBSIDIARIES                  | (7,133)                                  | 5,974    | (10,807)                  | 24,233                        |              | 12,267       |
| EQUITY IN NET INCOME OF SUBSIDIARIES                                       | 19,234                                   |          | 31,187                    |                               | (50,421)     |              |
| INCOME FROM CONTINUING OPERATIONS  | 12,101                                   | 5,974    | 20,380                    | 24,233                        | (50,421)     | 12,267       |
| LOSS FROM DISCONTINUED OPERATIONS, net of tax                              |  |          |                           |                               | (166)        | (166)        |
| NET INCOME   | \$ 12,101                                | \$ 5,974 | \$ 20,380                 | \$ 24,067                     | \$ (50,421)  | \$ 12,101    |

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**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**  
**CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS**

(in thousands)

|  | For the Six Months Ended June 30, 2007 |          |                           |                               |              |              |
|--|--|----------|---------------------------|-------------------------------|--------------|--------------|
|  | PTGI                                   | IHC      | Guarantor<br>Subsidiaries | Non Guarantor<br>Subsidiaries | Eliminations | Consolidated |
| NET REVENUE  | \$                                     | \$       | \$ 73,996                 | \$ 378,437                    | \$           | \$ 452,433   |
| OPERATING EXPENSES   |  |          |                           |                               |              |              |
| Cost of revenue (exclusive of depreciation included below)                 |  |          | 53,105                    | 232,554                       |              | 285,659      |
| Selling, general and administrative  | 2,498                                  | 54       | 23,191                    | 110,469                       |              | 136,212      |
| Depreciation and amortization  |  |          | 1,896                     | 12,004                        |              | 13,900       |
| Loss on sale or disposal of assets   |  |          | 8                         | 676                           |              | 684          |
| Total operating expenses   | 2,498                                  | 54       | 78,200                    | 355,703                       |              | 436,455      |
| INCOME (LOSS) FROM OPERATIONS  | (2,498)                                | (54)     | (4,204)                   | 22,734                        |              | 15,978       |
| INTEREST EXPENSE   | (5,803)                                | (4,311)  | (15,805)                  | (3,939)                       |              | (29,858)     |
| ACCRETION ON DEBT PREMIUM (DISCOUNT)                                       | (791)                                  |          |                           | 417                           |              | (374)        |
| LOSS ON EARLY EXTINGUISHMENT OR RESTRUCTURING OF DEBT                      | (2,311)                                | (5,050)  | (4)                       | (909)                         |              | (8,274)      |
| INTEREST AND OTHER INCOME  | 334                                    |          | 29                        | 2,191                         |              | 2,554        |
| FOREIGN CURRENCY TRANSACTION GAIN  | 3,848                                  | 4,486    | 486                       | 9,235                         |              | 18,055       |
| INTERCOMPANY INTEREST  | (673)                                  | 4,229    | (5,184)                   | 1,628                         |              |              |
| MANAGEMENT FEE   |  |          | 3,522                     | (3,522)                       |              |              |
| ROYALTY FEE  |  | 7,145    | (297)                     | (6,848)                       |              |              |
| INCOME (LOSS) BEFORE INCOME TAXES AND EQUITY IN NET INCOME OF SUBSIDIARIES | (7,894)                                | 6,445    | (21,457)                  | 20,987                        |              | (1,919)      |
| INCOME TAX BENEFIT (EXPENSE)   | 2,472                                  | (1,023)  | (409)                     | 4,646                         |              | 5,686        |
| INCOME (LOSS) BEFORE EQUITY IN NET INCOME OF SUBSIDIARIES                  | (5,422)                                | 5,422    | (21,866)                  | 25,633                        |              | 3,767        |
| EQUITY IN NET INCOME OF SUBSIDIARIES                                       | 14,881                                 |          | 39,033                    |                               | (53,914)     |              |
| INCOME FROM CONTINUING OPERATIONS  | 9,459                                  | 5,422    | 17,167                    | 25,633                        | (53,914)     | 3,767        |
| LOSS FROM DISCONTINUED OPERATIONS, net of tax                              |  |          |                           | (266)                         |              | (266)        |
| GAIN ON SALE OF DISCONTINUED OPERATIONS, net of tax                        |  |          |                           | 5,958                         |              | 5,958        |
| NET INCOME   | \$ 9,459                               | \$ 5,422 | \$ 17,167                 | \$ 31,325                     | \$ (53,914)  | \$ 9,459     |



**Table of Contents****PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED****CONSOLIDATING CONDENSED BALANCE SHEET**

(in thousands )

|  | June 30 , 2008 |            |                           |                               |                |              |
|--|----------------|------------|---------------------------|-------------------------------|----------------|--------------|
|  | PTGI           | IHC        | Guarantor<br>Subsidiaries | Non Guarantor<br>Subsidiaries | Eliminations   | Consolidated |
| <b>ASSETS</b>                                  |                |            |                           |                               |                |              |
| <b>CURRENT ASSETS:</b>                         |                |            |                           |                               |                |              |
| Cash and cash equivalents                      | \$ 4,810       | \$         | \$ 243                    | \$ 50,497                     | \$             | \$ 55,550    |
| Accounts receivable                            |                |            | 14,272                    | 104,140                       |                | 118,412      |
| Prepaid expenses and other current assets      | 123            |            | 1,150                     | 18,197                        |                | 19,470       |
| Total current assets                           | 4,933          |            | 15,665                    | 172,834                       |                | 193,432      |
| INTERCOMPANY RECEIVABLES                       | 96,854         | 297,296    | 593,089                   | 63,453                        | (1,050,692)    |              |
| INVESTMENTS IN SUBSIDIARIES                    | 41,447         |            | (45,071)                  |                               | 3,624          |              |
| RESTRICTED CASH                                |                |            | 314                       | 10,468                        |                | 10,782       |
| PROPERTY AND EQUIP MENT Net                    |                |            | 14,650                    | 133,103                       |                | 147,753      |
| GOODWILL                                       |                |            |                           | 40,539                        |                | 40,539       |
| OTHER INTANGIBLE ASSETS Net                    |                |            |                           | 989                           |                | 989          |
| OTHER ASSETS                                   | 527            | 272        | 6,250                     | 26,382                        |                | 33,431       |
| TOTAL ASSETS                                   | \$ 143,761     | \$ 297,568 | \$ 584,897                | \$ 447,768                    | \$ (1,047,068) | \$ 426,926   |
| <b>LIABILITIES AND STOCKHOLDERS</b>            |                |            |                           |                               |                |              |
| <b>EQUITY (DEFICIT)</b>                        |                |            |                           |                               |                |              |
| <b>CURRENT LIABILITIES:</b>                    |                |            |                           |                               |                |              |
| Accounts payable                               | \$ 359         | \$         | \$ 4,403                  | \$ 55,572                     | \$             | \$ 60,334    |
| Accrued interconnection costs                  |                |            | 17,556                    | 31,840                        |                | 49,396       |
| Deferred revenue                               |                |            | 1,069                     | 14,770                        |                | 15,839       |
| Accrued expenses and other current liabilities | 274            | 460        | 6,648                     | 46,136                        |                | 53,518       |
| Accrued income taxes                           | 85             | 3,946      | 1,007                     | 21,284                        |                | 26,322       |
| Accrued interest                               | 1,173          | 1,387      | 8,468                     | 163                           |                | 11,191       |
| Current portion of long-term obligations       |                |            | 2,260                     | 7,041                         |                | 9,301        |
| Total current liabilities                      | 1,891          | 5,793      | 41,411                    | 176,806                       |                | 225,901      |
| INTERCOMPANY PAYABLES                          | 493,361        |            | 195,601                   | 361,730                       | (1,050,692)    |              |
| LONG-TERM OBLIGATIONS                          | 56,440         | 206,744    | 306,438                   | 39,254                        |                | 608,876      |
| OTHER LIABILITIES                              |                |            |                           | 80                            |                | 80           |
| Total liabilities                              | 551,692        | 212,537    | 543,450                   | 577,870                       | (1,050,692)    | 834,857      |
| <b>COMMITMENTS AND CONTINGENCIES</b>           |                |            |                           |                               |                |              |
| <b>STOCKHOLDERS EQUITY (DEFICIT):</b>          |                |            |                           |                               |                |              |
| Common stock                                   | 1,426          |            |                           |                               |                | 1,426        |
| Additional paid-in capital                     | 718,827        |            | 1,161,930                 | 306,227                       | (1,468,157)    | 718,827      |
| Retained earnings (accumulated deficit)        | (1,031,253)    | 85,031     | (1,024,352)               | (344,158)                     | 1,283,479      | (1,031,253)  |
| Accumulated other comprehensive loss           | (96,931)       |            | (96,131)                  | (92,171)                      | 188,302        | (96,931)     |
| Total stockholders equity (deficit)            | (407,931)      | 85,031     | 41,447                    | (130,102)                     | 3,624          | (407,931)    |

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|  |            |            |            |            |                |            |
|--|------------|------------|------------|------------|----------------|------------|
| TOTAL LIABILITIES AND STOCKHOLDERS<br>EQUITY (DEFICIT) | \$ 143,761 | \$ 297,568 | \$ 584,897 | \$ 447,768 | \$ (1,047,068) | \$ 426,926 |
|--|------------|------------|------------|------------|----------------|------------|

**Table of Contents****PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED****CONSOLIDATING CONDENSED BALANCE SHEET**

(in thousands)

|  | December 31, 2007 |                   |                           |                               |                     |                   |
|--|-------------------|-------------------|---------------------------|-------------------------------|---------------------|-------------------|
|  | PTGI              | IHC               | Guarantor<br>Subsidiaries | Non Guarantor<br>Subsidiaries | Eliminations        | Consolidated      |
| <b>ASSETS</b>  |                   |                   |                           |                               |                     |                   |
| <b>CURRENT ASSETS:</b>                                     |                   |                   |                           |                               |                     |                   |
| Cash and cash equivalents                                  | \$ 1,299          | \$                | \$ 670                    | \$ 79,313                     | \$                  | \$ 81,282         |
| Restricted cash  |                   |                   |                           | 362                           |                     | 362               |
| Accounts receivable  |                   |                   | 14,002                    | 99,586                        |                     | 113,588           |
| Prepaid expenses and other current assets                  | 308               |                   | 1,255                     | 27,097                        |                     | 28,660            |
| <b>Total current assets</b>                                | <b>1,607</b>      |                   | <b>15,927</b>             | <b>206,358</b>                |                     | <b>223,892</b>    |
| INTERCOMPANY RECEIVABLES                                   | 88,536            | 195,254           | 601,606                   | 18,779                        | (904,175)           |                   |
| INVESTMENTS IN SUBSIDIARIES                                | 5,404             |                   | (76,945)                  |                               | 71,541              |                   |
| RESTRICTED CASH  |                   |                   | 314                       | 9,363                         |                     | 9,677             |
| PROPERTY AND EQUIPMENT Net                                 |                   |                   | 15,881                    | 128,718                       |                     | 144,599           |
| GOODWILL   |                   |                   |                           | 40,134                        |                     | 40,134            |
| OTHER INTANGIBLE ASSETS Net                                |                   |                   |                           | 1,557                         |                     | 1,557             |
| OTHER ASSETS   | 2,389             | 283               | 8,261                     | 29,611                        |                     | 40,544            |
| <b>TOTAL ASSETS</b>  | <b>\$ 97,936</b>  | <b>\$ 195,537</b> | <b>\$ 565,044</b>         | <b>\$ 434,520</b>             | <b>\$ (832,634)</b> | <b>\$ 460,403</b> |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY (DEFICIT)</b>       |                   |                   |                           |                               |                     |                   |
| <b>CURRENT LIABILITIES:</b>                                |                   |                   |                           |                               |                     |                   |
| Accounts payable   | \$ 805            | \$                | \$ 4,889                  | \$ 69,199                     | \$                  | \$ 74,893         |
| Accrued interconnection costs                              |                   |                   | 15,200                    | 29,711                        |                     | 44,911            |
| Deferred revenue   |                   |                   | 969                       | 15,544                        |                     | 16,513            |
| Accrued expenses and other current liabilities             | 207               |                   | 8,458                     | 45,755                        |                     | 54,420            |
| Accrued income taxes                                       | 306               | 4,656             | 2,278                     | 23,551                        |                     | 30,791            |
| Accrued interest   | 2,388             | 1,328             | 8,701                     | 43                            |                     | 12,460            |
| Current portion of long-term obligations                   |                   |                   | 3,908                     | 7,320                         |                     | 11,228            |
| <b>Total current liabilities</b>                           | <b>3,706</b>      | <b>5,984</b>      | <b>44,403</b>             | <b>191,123</b>                |                     | <b>245,216</b>    |
| INTERCOMPANY PAYABLES                                      | 424,978           |                   | 123,276                   | 355,921                       | (904,175)           |                   |
| LONG-TERM OBLIGATIONS                                      | 116,792           | 113,947           | 391,961                   | 39,975                        |                     | 662,675           |
| OTHER LIABILITIES  |                   |                   |                           | 52                            |                     | 52                |
| <b>Total liabilities</b>                                   | <b>545,476</b>    | <b>119,931</b>    | <b>559,640</b>            | <b>587,071</b>                | <b>(904,175)</b>    | <b>907,943</b>    |
| <b>COMMITMENTS AND CONTINGENCIES</b>                       |                   |                   |                           |                               |                     |                   |
| <b>STOCKHOLDERS EQUITY (DEFICIT):</b>                      |                   |                   |                           |                               |                     |                   |
| Common stock   | 1,426             |                   |                           |                               |                     | 1,426             |
| Additional paid-in capital                                 | 718,695           |                   | 1,161,930                 | 305,937                       | (1,467,867)         | 718,695           |
| Retained earnings (accumulated deficit)                    | (1,074,778)       | 75,606            | (1,064,443)               | (370,365)                     | 1,359,202           | (1,074,778)       |
| Accumulated other comprehensive loss                       | (92,883)          |                   | (92,083)                  | (88,123)                      | 180,206             | (92,883)          |
| <b>Total stockholders equity (deficit)</b>                 | <b>(447,540)</b>  | <b>75,606</b>     | <b>5,404</b>              | <b>(152,551)</b>              | <b>71,541</b>       | <b>(447,540)</b>  |
| <b>TOTAL LIABILITIES AND STOCKHOLDERS EQUITY (DEFICIT)</b> | <b>\$ 97,936</b>  | <b>\$ 195,537</b> | <b>\$ 565,044</b>         | <b>\$ 434,520</b>             | <b>\$ (832,634)</b> | <b>\$ 460,403</b> |



**Table of Contents****PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED****CONSOLIDATING CONDENSED STATEMENT OF CASH FLOWS**

(in thousands)

|  | For Six Months Ended June 30, 2008 |          |                           |                               |              | Consolidated |
|--|------------------------------------|----------|---------------------------|-------------------------------|--------------|--------------|
|  | PTGI                               | IHC      | Guarantor<br>Subsidiaries | Non Guarantor<br>Subsidiaries | Eliminations |              |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>   |                                    |          |                           |                               |              |              |
| Net income   | \$ 43,525                          | \$ 9,425 | \$ 38,519                 | \$ 26,497                     | \$ (74,441)  | \$ 43,525    |
| Adjustments to reconcile net income to net cash provided by operating activities:                                |                                    |          |                           |                               |              |              |
| Provision for doubtful accounts receivable   |                                    |          | 1,132                     | 4,564                         |              | 5,696        |
| Stock compensation expense   |                                    |          | 132                       |                               |              | 132          |
| Depreciation and amortization  |                                    |          | 1,681                     | 14,375                        |              | 16,056       |
| Gain on sale or disposal of assets   |                                    |          | (805)                     | (1,660)                       |              | (2,465)      |
| Accretion of debt (premium) discount   | 512                                | (699)    |                           |                               |              | (187)        |
| Equity in net (income) loss of subsidiary  | (40,091)                           |          | (34,350)                  |                               | 74,441       |              |
| Deferred income taxes  |                                    |          | 591                       | 2,254                         |              | 2,845        |
| (Gain) loss on early extinguishment or restructuring of debt   | (12,070)                           | 475      | (22,784)                  | (108)                         |              | (34,487)     |
| Unrealized foreign currency transaction gain on intercompany and foreign debt                                    | (2,684)                            | (3,249)  | (487)                     | (3,208)                       |              | (9,628)      |
| Changes in assets and liabilities, net of acquisitions:  |                                    |          |                           |                               |              |              |
| Increase in accounts receivable  |                                    |          | (1,403)                   | (4,985)                       |              | (6,388)      |
| Decrease in prepaid expenses and other current assets  | 185                                |          | 106                       | 10,943                        |              | 11,234       |
| (Increase) decrease in other assets  | 388                                | 11       | 518                       | (12)                          |              | 905          |
| (Increase) decrease in intercompany balance  |                                    | (4,499)  | (6,218)                   | 10,717                        |              |              |
| Decrease in accounts payable   | (447)                              |          | (486)                     | (15,706)                      |              | (16,639)     |
| Increase in accrued interconnection costs  |                                    |          | 2,355                     | 804                           |              | 3,159        |
| Increase (decrease), net, in deferred revenue, accrued expenses, other current liabilities and other liabilities | 67                                 | (4)      | (1,718)                   | (1,424)                       |              | (3,079)      |
| Decrease in accrued income taxes   | (222)                              | (710)    | (1,271)                   | (2,252)                       |              | (4,455)      |
| Increase (decrease) in accrued interest  | (871)                              | 59       | (223)                     | 114                           |              | (921)        |
| Net cash provided by (used in) operating activities  | (11,708)                           | 809      | (24,711)                  | 40,913                        |              | 5,303        |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>   |                                    |          |                           |                               |              |              |
| Purchase of property and equipment   |                                    |          | (450)                     | (14,149)                      |              | (14,599)     |
| Sale of property and equipment   |                                    |          | 805                       |                               |              | 805          |
| Cash from disposition of business, net of cash disposed  |                                    |          |                           | 1,676                         |              | 1,676        |
| Cash used for business acquisitions, net of cash acquired  |                                    |          |                           | (34)                          |              | (34)         |
| Decrease in restricted cash  |                                    |          |                           | 103                           |              | 103          |
| Proceeds from intercompany balance   | 27,636                             |          | 14,409                    |                               | (42,045)     |              |
| Net cash provided by (used in) investing activities  | 27,636                             |          | 14,764                    | (12,404)                      | (42,045)     | (12,049)     |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>   |                                    |          |                           |                               |              |              |
| Purchase of the Company's debt securities  | (11,217)                           |          |                           |                               |              | (11,217)     |
| Principal payments on other long-term obligations  | (1,200)                            | (3)      | (5,245)                   | (1,839)                       |              | (8,287)      |
| Proceeds from (payments on) intercompany balance   |                                    | (806)    | 14,765                    | (56,004)                      | 42,045       |              |
| Net cash provided by (used in) financing activities  | (12,417)                           | (809)    | 9,520                     | (57,843)                      | 42,045       | (19,504)     |
| <b>EFFECTS OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>   |                                    |          |                           |                               |              |              |
|  |                                    |          |                           | 518                           |              | 518          |
| NET CHANGE IN CASH AND CASH EQUIVALENTS  | 3,511                              |          | (427)                     | (28,816)                      |              | (25,732)     |
|  | 1,299                              |          | 670                       | 79,313                        |              | 81,282       |

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CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD

|  |    |       |    |  |    |     |    |        |    |  |    |        |
|--|----|-------|----|--|----|-----|----|--------|----|--|----|--------|
| CASH AND CASH EQUIVALENTS, END OF PERIOD | \$ | 4,810 | \$ |  | \$ | 243 | \$ | 50,497 | \$ |  | \$ | 55,550 |
|--|----|-------|----|--|----|-----|----|--------|----|--|----|--------|

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**PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED**  
**CONSOLIDATING CONDENSED STATEMENT OF CASH FLOWS**

(in thousands)

|  | For the Six Months Ended June 30, 2007 |              |                           |                           |                  |                 |
|--|--|--------------|---------------------------|---------------------------|------------------|-----------------|
|  |  |              | Non                       |                           |                  |                 |
|  | PTGI                                   | IHC          | Guarantor<br>Subsidiaries | Guarantor<br>Subsidiaries | Eliminations     | Consolidated    |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>   |  |              |                           |                           |                  |                 |
| Net income   | \$ 9,459                               | \$ 5,422     | \$ 17,167                 | \$ 31,325                 | \$ (53,914)      | \$ 9,459        |
| Adjustments to reconcile net income to net cash provided by operating activities:  |  |              |                           |                           |                  |                 |
| Provision for doubtful accounts receivable   |  |              | 599                       | 4,286                     |                  | 4,885           |
| Stock compensation expense   |  |              | 125                       |                           |                  | 125             |
| Depreciation and amortization  |  |              | 1,896                     | 12,050                    |                  | 13,946          |
| (Gain) loss on sale or disposal of assets  |  |              | 8                         | (5,086)                   |                  | (5,078)         |
| Accretion of debt (premium) discount   | 791                                    | (417)        |                           |                           |                  | 374             |
| Equity in net gain of subsidiary   | (14,881)                               |              | (39,033)                  |                           | 53,914           |                 |
| Loss on early extinguishment or restructuring of debt  | 2,311                                  | 5,050        | 4                         | 909                       |                  | 8,274           |
| Unrealized foreign currency transaction gain on intercompany and foreign debt  | (7,550)                                | (2,997)      | (2,194)                   | (6,766)                   |                  | (19,507)        |
| Changes in assets and liabilities, net of acquisitions:  |  |              |                           |                           |                  |                 |
| (Increase) decrease in accounts receivable   |  |              | 3,669                     | (2,641)                   |                  | 1,028           |
| Decrease in prepaid expenses and other current assets  | 93                                     |              | 86                        | 1,874                     |                  | 2,053           |
| (Increase) decrease in other assets  | 460                                    | 19           | 903                       | (1,488)                   |                  | (106)           |
| (Increase) decrease in intercompany balance  |  | (8,325)      | (838)                     | 9,163                     |                  |                 |
| Increase (decrease) in accounts payable  | (287)                                  |              | (2,141)                   | 1,872                     |                  | (556)           |
| Decrease in accrued interconnection costs  |  |              | (4,579)                   | (66)                      |                  | (4,645)         |
| Increase (decrease), net, in deferred revenue, accrued expenses, other current liabilities, accrued income taxes and other liabilities | (3,242)                                | 729          | 343                       | (1,745)                   |                  | (3,915)         |
| Increase (decrease) in accrued interest  | (1,581)                                | 1,328        | (97)                      | (679)                     |                  | (1,029)         |
| <b>Net cash provided by (used in) operating activities</b>   | <b>(14,427)</b>                        | <b>809</b>   | <b>(24,082)</b>           | <b>43,008</b>             |                  | <b>5,308</b>    |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>   |  |              |                           |                           |                  |                 |
| Purchase of property and equipment   |  |              | (454)                     | (16,587)                  |                  | (17,041)        |
| Cash from disposition of business, net of cash disposed  |  |              |                           | 5,527                     |                  | 5,527           |
| Decrease in restricted cash  |  |              | 541                       | 55                        |                  | 596             |
| Increase (decrease) in intercompany balance  | 69,530                                 |              | 36,956                    |                           | (106,486)        |                 |
| <b>Net cash provided by (used in) investing activities</b>   | <b>69,530</b>                          |              | <b>37,043</b>             | <b>(11,005)</b>           | <b>(106,486)</b> | <b>(10,918)</b> |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>   |  |              |                           |                           |                  |                 |
| Proceeds from issuance of long-term obligations  |  | 101,405      |                           | 7,870                     |                  | 109,275         |
| Deferred financing costs   |  |              |                           | (6,570)                   |                  | (6,570)         |
| Principal payments on capital leases, vendor financing and other long-term obligations   | (54,882)                               |              | (529)                     | (2,768)                   |                  | (58,179)        |
| Increase (decrease) in intercompany balance  |  | (102,214)    | (12,494)                  | 8,222                     | 106,486          |                 |
| <b>Net cash provided by (used in) financing activities</b>   | <b>(54,882)</b>                        | <b>(809)</b> | <b>(13,023)</b>           | <b>6,754</b>              | <b>106,486</b>   | <b>44,526</b>   |
| <b>EFFECTS OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>   |  |              |                           |                           |                  |                 |
|  |  |              |                           | 1,451                     |                  | 1,451           |
| <b>NET CHANGE IN CASH AND CASH EQUIVALENTS</b>   | <b>221</b>                             |              | <b>(62)</b>               | <b>40,208</b>             |                  | <b>40,367</b>   |
|  | 3,764                                  |              | (35)                      | 60,588                    |                  | 64,317          |

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CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD

|  |          |    |         |            |    |            |
|--|----------|----|---------|------------|----|------------|
| CASH AND CASH EQUIVALENTS, END OF PERIOD | \$ 3,985 | \$ | \$ (97) | \$ 100,796 | \$ | \$ 104,684 |
|--|----------|----|---------|------------|----|------------|



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**13. SUBSEQUENT EVENT**

In July 2008, a consolidated, variable interest entity in Canada of which the Company currently owns less than 50% of the equity, sold certain primarily rural WiMax spectrum (a spectrum for transmission of sound, data, and video) assets (representing approximately 10% of the entity's spectrum population coverage). The proceeds from the sale were \$4.9 million (\$5.0 million CAD).

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### **ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

#### **Introduction and Overview of Operations**

We are an integrated facilities based telecommunications services provider offering a portfolio of international and domestic voice, wireless, Internet, voice-over-Internet protocol (VOIP), data and hosting services to customers located primarily in the United States, Australia, Canada, the United Kingdom and western Europe. Our focus is to service the demand for high quality, competitively priced communications services that is being driven by the globalization of the world's economies, the worldwide trend toward telecommunications deregulation and the growth of broadband, Internet, VOIP, wireless and data traffic.

Generally, we price our services competitively with the major carriers and service providers operating in our principal service regions. We seek to generate net revenue through sales and marketing efforts focused on customers with significant communications needs, including small- and medium-sized enterprises (SMEs), multinational corporations, residential customers, and other telecommunications carriers and resellers and through acquisitions.

Our challenge to growing net revenue in recent years has been to overcome declines in long distance voice minutes of use per customer as more customers are using wireless devices and the Internet as alternatives to the use of wireline phones. Also, product substitution (e.g., wireless/Internet for fixed line voice; broadband for dial-up Internet service provider (ISP) services) has resulted in revenue declines in our legacy long distance voice and dial-up ISP businesses. Additionally, we believe that because deregulatory influences have begun to affect telecommunications markets outside the United States, the deregulatory trend is resulting in greater competition from the existing wireline and wireless competitors and from more recent entrants, such as cable companies and VOIP companies, which could continue to affect adversely our net revenue per minute, as well as minutes of use.

In order to manage our traffic network transmission costs, we pursue a flexible approach with respect to the management of our network capacity. In most instances, we optimize the cost of traffic by using the least expensive cost routing; negotiate lower variable usage based costs with domestic and foreign service providers and negotiate additional and lower cost foreign carrier agreements with the foreign incumbent carriers and others; and continue to expand/reduce the capacity of our network when traffic volumes justify such actions.

Our overall margin may fluctuate based on the relative volumes of international versus domestic long distance services; carrier services versus business and residential long distance services; prepaid services versus traditional post-paid voice services; Internet, VOIP and data services versus fixed line voice services; the amount of services that are resold; and the proportion of traffic carried on our network versus resale of other carriers' services. Our margin is also affected by customer transfer and migration fees. We generally pay a charge to install and transfer a new customer onto our network, and to migrate DSL and local customers. However, installing and migrating customers to our own networks, such as the local and DSL networks in Australia and Canada, enable us to increase our margin on such services as compared to resale of services using other carriers' networks.

SG&A expenses are comprised primarily of salaries and benefits, commissions, occupancy costs, sales and marketing expenses, advertising, professional fees, and administrative costs. All SG&A expenses are expensed when incurred. Emphasis on cost containment or the shift of expenditures from non-revenue producing expenses to sales and marketing expenses has been heightened since growth in net revenue has been under significant pressure.

#### **Second Quarter 2008 Results and Accomplishments**

Overall revenue increased in the first half of 2008 as compared to the same period a year ago. We have experienced declining usage and pricing in the legacy voice business, a decline in dial-up ISP services and a decline in low-margin prepaid services business. That revenue decline has been offset by increases in

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our wholesale sales and the continued growth of our higher margin broadband, VOIP, local, wireless, data and hosting services revenues, which in the second quarter 2008 are at an annualized net revenue run rate of approximately \$247 million. Our objective is to continue to generate increased contribution from these products that exceeds the declines in legacy voice and dial-up Internet products. Our future growth and profitability are dependent upon accomplishing that goal.

We are encouraged by our second consecutive quarter of net revenue growth, and we are targeting slight year-over-year revenue growth for 2008. We are also pleased that continued increases in our growth products have eclipsed the decline in legacy services during the first two quarters of 2008. Growth in net revenue, together with continued cost management, has generated \$15.3 million in income from operations, up sharply from \$9.8 million in the first quarter. When excluding \$5.8 million from a regulatory award involving excessive pricing by Telstra (see ACCC Ruling below) in this quarter and the \$2.6 million gain on sale of assets in the first quarter, income from operations increased sequentially by 32%.

During the first two quarters of 2008, we accomplished the following: opened new, and expanded existing, data centers in Canada and Australia; expanded the global DSLAM footprint by 20 to a total of 303 to expand the availability of our local and broadband services; augmented network capacity to offer higher speed DSL services in Australia and Canada; and continued growth of the Company's direct sales force and telemarketing capabilities across its major markets. As the currently available capacity through our infrastructure investment is adequate to meet our 2008 revenue goals, we now expect capital expenditures for the year to be in the \$25 million to \$30 million range, approximately \$5 million lower than our prior guidance.

During the first quarter, we purchased and retired \$15 million principal amount of the Company's outstanding debt maturing in the latter half of 2009. We also completed the sales of a minority equity investment in a Japanese entity and surplus fiber assets for an aggregate \$2.6 million in cash proceeds. During the second quarter, we reduced outstanding debt principal by \$63.2 million through private exchange transactions. We successfully issued \$67.1 million principal amount of new debt plus \$4.7 million in cash in exchange for \$130.3 million principal amount of outstanding debt. These transactions and normal debt amortization payments reduced overall debt principal levels from \$664.3 million at December 31, 2007 to \$585.0 million at the end of the second quarter 2008, reduced debt maturing in the latter half of 2009 from \$28.1 million to \$22.8 million, and reduced debt maturing in the latter half of 2010 from \$133.6 million to \$57.6 million.

Subsequent to the end of the second quarter, a consolidated, variable interest entity in Canada, of which the Company currently owns slightly less than 50% of the equity, sold certain primarily rural WIMAX spectrum (spectrum for transmission of sound, data, and video) assets (representing approximately 10% of the entity's spectrum population coverage) for cash consideration of \$4.9 million (\$5.0 million CAD).

### **ACCC Ruling**

In April 2008, the Australian Competition and Consumer Commission (ACCC) issued a Final Determination related to unconditional local loop services connection and call diversion charges (2008 ACCC Ruling). As a result, we received a \$6.2 million (\$6.5 million AUD) cash refund in June 2008 of a portion of fees previously paid, plus interest. Of the \$6.2 million refund, \$5.8 million was recognized as a reduction to cost of revenue.

### **PRIMUS 2007-2008 Transformation Strategy**

In light of improved operating performance over the course of 2006, we announced a two-year Transformation Strategy as we entered 2007. One of our major priorities was to resume top line revenue growth before the end of 2008. With two successive quarters of top line revenue growth and with our adjusted guidance now targeting positive revenue growth for the full year 2008 over the prior year, assuming constant currency rates, we are on trajectory to meet this goal.

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We also emphasized the need to strengthen our balance sheet significantly. At December 31, 2006, we had \$639.6 million of debt principal outstanding. Through a series of subsequent debt issuances and exchanges we have reduced that figure to \$585.0 million at June 30, 2008. Significantly, that net debt reduction was accompanied with an improvement to liquidity from sales of debt and equity, a more favorable schedule of maturities, and no material increase in cash interest obligations. However, while the Company has made substantial progress in strengthening its balance sheet, more needs to be accomplished.

Generating double digit annual growth in income from operations was another critical objective of the strategy. Our operating improvements reflect the execution of the following sub-strategies:

- A) Focus on improving sales productivity and margin enhancements by leveraging our network assets and increasing the revenue mix in favor of higher margin growth services; and
- B) Significantly improving our non-sales and marketing cost structure through increased outsourcing and/or off-shoring at lower cost locations globally and maintaining an aggressive cost management program.

While we continue to pursue the goal to sell select assets to improve liquidity as well as to narrow our geographic focus to our major franchises, prevailing uncertainty in the capital markets combined with a weak overall economic outlook is likely to extend our time horizon to meet the goal of generating \$50 million in cash proceeds, particularly if valuation parameters are not at acceptable levels.

## **Foreign Currency**

Foreign currency can have a major impact on our financial results. Currently in excess of 81% of our net revenue is derived from sales and operations outside the United States. The reporting currency for our consolidated financial statements is the United States dollar (USD). The local currency of each country is the functional currency for each of our respective entities operating in that country. In the future, we expect to continue to derive the majority of our net revenue and incur a significant portion of our operating costs from outside the United States, and therefore changes in exchange rates have had and may continue to have a significant, and potentially adverse, effect on our results of operations. Our primary risk of loss regarding foreign currency exchange rate risk is caused primarily by fluctuations in the following exchange rates: USD/Canadian dollar (CAD), USD/Australian dollar (AUD), USD/British pound (GBP), and USD/Euro (EUR). Due to the large percentage of our revenue derived outside of the United States, changes in the USD relative to one or more of the foregoing currencies could have an adverse impact on our future results of operations. We have agreements with certain subsidiaries for repayment of a portion of the investments and advances made to these subsidiaries. As we anticipate repayment in the foreseeable future, we recognize the unrealized gains and losses in foreign currency transaction gain (loss) on the consolidated statements of operations. We historically have not engaged in hedging transactions. However, during the fourth quarter 2007, we completed a forward currency contract required by the Canadian Credit Agreement and an interest rate swap. The exposure of our income from operations to fluctuations in foreign currency exchange rates is reduced in part because a majority of the costs that we incur in connection with our foreign operations are also denominated in local currencies. Given the recent volatility in exchange rates affecting the functional currencies in our major markets as compared to the USD, we will continue to explore whether hedging activities may provide benefit to us.

We are exposed to financial statement gains and losses as a result of translating the operating results and financial position of our international subsidiaries. We translate the local currency statements of operations of our foreign subsidiaries into USD using the average exchange rate during the reporting period. Changes in foreign exchange rates affect the reported profits and losses and cash flows and may distort comparisons from year to year. By way of example, when the USD strengthens compared to the EUR, there could be a negative or positive effect on the reported results for Europe, depending upon whether Europe is operating profitably or at a loss. It takes more profits in EUR to generate the same amount of profits in USD and a greater loss in EUR to generate the same amount of loss in USD. The opposite is also true. For instance, when the USD weakens there is a positive effect on reported profits and a negative effect on the reported losses for Europe.

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In the three months and six months ended June 30, 2008, as compared to the three months and six months ended June 30, 2007, the USD was weaker on average as compared to the CAD, AUD, GBP and EUR. The following tables demonstrate the impact of currency fluctuations on our net revenue for the three months and six months ended June 30, 2008 and 2007 (in thousands, except percentages):

## Net Revenue by Location in USD

|                | For the three months ended June 30, |           |            |            | For the six months ended June 30, |            |             |            |
|----------------|-------------------------------------|-----------|------------|------------|-----------------------------------|------------|-------------|------------|
|                | 2008                                | 2007      | Variance   | Variance % | 2008                              | 2007       | Variance    | Variance % |
| Canada         | \$ 68,989                           | \$ 63,588 | \$ 5,401   | 8%         | \$ 137,438                        | \$ 126,372 | \$ 11,066   | 9%         |
| Australia      | \$ 75,992                           | \$ 71,950 | \$ 4,042   | 6%         | \$ 150,066                        | \$ 142,151 | \$ 7,915    | 6%         |
| United Kingdom | \$ 22,204                           | \$ 25,100 | \$ (2,896) | (12)%      | \$ 39,581                         | \$ 49,973  | \$ (10,392) | (21)%      |
| Europe*        | \$ 22,603                           | \$ 19,660 | \$ 2,943   | 15%        | \$ 42,654                         | \$ 38,993  | \$ 3,661    | 9%         |

## Net Revenue by Location in Local Currencies

|                         | For the three months ended June 30, |        |          |            | For the six months ended June 30, |         |          |            |
|-------------------------|-------------------------------------|--------|----------|------------|-----------------------------------|---------|----------|------------|
|                         | 2008                                | 2007   | Variance | Variance % | 2008                              | 2007    | Variance | Variance % |
| Canada (in CAD)         | 69,710                              | 69,951 | (241)    | (0)%       | 138,473                           | 143,542 | (5,069)  | (4)%       |
| Australia (in AUD)      | 80,598                              | 86,643 | (6,045)  | (7)%       | 162,494                           | 176,026 | (13,532) | (8)%       |
| United Kingdom (in GBP) | 11,268                              | 13,257 | (1,989)  | (15)%      | 20,054                            | 26,788  | (6,734)  | (25)%      |
| Europe* (in EUR)        | 14,466                              | 14,582 | (116)    | (1)%       | 27,844                            | 29,342  | (1,498)  | (5)%       |

\* Europe includes only subsidiaries whose functional currency is the Euro dollar.

**Critical Accounting Policies**

See Management's Discussion and Analysis of Financial Condition and Results of Operations in our Form 10-K for the year ended December 31, 2007 for a detailed discussion of our critical accounting policies. These policies include revenue recognition, determining our allowance for doubtful accounts receivable, accounting for cost of revenue, valuation of long-lived assets and goodwill and accounting for income taxes. No significant changes in our critical accounting policies have occurred since December 31, 2007.

**Results of Operations****Results of operations for the three months ended June 30, 2008 as compared to the three months ended June 30, 2007**

Net revenue increased \$10.0 million or 4.4% to \$236.5 million for the three months ended June 30, 2008 from \$226.4 million for the three months ended June 30, 2007. Our revenue from broadband, VOIP, local, wireless, data and hosting services contributed \$61.8 million for the three months ended June 30, 2008, as compared to \$53.3 million for the three months ended June 30, 2007. Our wholesale carrier and prepaid services contributed \$48.9 million and \$10.1 million, respectively, for the three months ended June 30, 2008, as compared to \$43.5 million and \$11.6 million, respectively, for the three months ended June 30, 2007.

United States: United States retail net revenue decreased \$3.2 million or 11.6% to \$25.1 million for the three months ended June 30, 2008 from \$28.4 million for the three months ended June 30, 2007. The decrease is primarily attributed to a decrease of \$4.0 million in retail voice services and a decrease of \$0.3 million in Internet services, offset by an increase of \$1.0 million in retail VOIP.

Canada: Canada retail net revenue increased \$5.5 million or 8.6% to \$69.0 million for the three months ended June 30, 2008 from \$63.5 million for the three months ended June 30, 2007. The increase is primarily attributed to an increase of \$3.9 million in Internet, data and hosting services, an increase of \$1.8 million in local service,

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an increase of \$0.5 million in VOIP services and an increase of \$0.3 million in wireless services. These increases were partially offset by a decrease of \$0.2 million in prepaid services and a decrease of \$0.9 million in retail voice services. The strengthening of the CAD against the USD accounted for a \$5.6 million increase to revenue, which is included in the explanations above, and which reflects changes in the exchange rates for the three months ended June 30, 2008 as compared to the three months ended June 30, 2007.

The following table reflects net revenue for each major country in North America (in thousands, except percentages):

Revenue by Country (Excluding Wholesale) in USD

|               | For the Three Months Ended |               | Year-over-Year |            |
|---------------|----------------------------|---------------|----------------|------------|
|               | June 30, 2008              | June 30, 2007 | Variance       | Variance % |
|               | Net Revenue                | Net Revenue   |                |            |
| United States | \$ 22,445                  | \$ 26,831     | \$ (4,386)     | (16)%      |
| Canada        | \$ 68,989                  | \$ 63,500     | \$ 5,489       | 9%         |
| Other         | \$ 2,680                   | \$ 1,521      | \$ 1,159       | 76%        |

Europe: European retail net revenue decreased \$1.5 million or 8.2% to \$16.9 million for the three months ended June 30, 2008 from \$18.4 million for the three months ended June 30, 2007. The decrease is primarily attributable to a decrease of \$1.7 million in retail voice services and a \$0.4 million decrease in wireless services, offset by a \$0.6 million increase in retail VOIP. The strengthening of the European currencies against the USD accounted for a \$1.3 million increase to revenue, which is included in the explanations above, when comparing the exchange rates for the three months ended June 30, 2008 as compared to the three months ended June 30, 2007.

The following table reflects net revenue for each major country in Europe (in thousands, except percentages):

Revenue by Country (Excluding Wholesale) in USD

|                | For the Three Months Ended June 30, 2008 |             | For the Three Months Ended June 30, 2007 |             | Year-over-Year |            |
|----------------|--|-------------|--|-------------|----------------|------------|
|                | Net Revenue                              | % of Europe | Net Revenue                              | % of Europe | Variance       | Variance % |
|                |  |             |  |             |                |            |
| United Kingdom | \$ 6,786                                 | 40%         | \$ 11,612                                | 63%         | \$ (4,826)     | (42)%      |
| France         | 5,050                                    | 30%         | 2,503                                    | 14%         | 2,547          | 102%       |
| Belgium        | 2,141                                    | 13%         | 2,436                                    | 13%         | (295)          | (12)%      |
| Spain          | 1,015                                    | 6%          | 1,149                                    | 6%          | (134)          | (12)%      |
| Other          | 1,933                                    | 11%         | 731                                      | 4%          | 1,202          | 164%       |
| Europe Total   | \$ 16,925                                | 100%        | \$ 18,431                                | 100%        | \$ (1,506)     | (8)%       |

Asia-Pacific: Asia-Pacific net revenue increased \$3.9 million or 5.4% to \$76.6 million for the three months ended June 30, 2008 from \$72.6 million for the three months ended June 30, 2007. The increase is primarily attributable to a \$1.8 million increase in Australia DSL services, a \$3.6 million increase in Australia business and residential voice services, and a \$0.3 million increase in wireless services, partially offset by an \$1.1 million decrease in dial-up Internet services. The strengthening of the AUD against the USD accounted for a \$9.7 million increase to revenue, which is included in the explanations above, which reflects changes in the exchange rates for the three months ended June 30, 2008 as compared to the three months ended June 30, 2007.

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The following table reflects net revenue for each major country in Asia-Pacific (in thousands, except percentages):

Revenue by Country (Excluding Wholesale) in USD

|                           | For the Three Months Ended<br>June 30, 2008 |                      | For the Three Months Ended<br>June 30, 2007 |                      | Year-over-Year  |            |
|---------------------------|---|----------------------|---|----------------------|-----------------|------------|
|                           | Net<br>Revenue                              | % of<br>Asia-Pacific | Net<br>Revenue                              | % of<br>Asia-Pacific | Variance        | Variance % |
| Australia                 | \$ 75,992                                   | 99%                  | \$ 71,950                                   | 99%                  | \$ 4,042        | 6%         |
| Other                     | 565   | 1%                   | 680   | 1%                   | (115)           | (17)%      |
| <b>Asia-Pacific Total</b> | <b>\$ 76,557</b>                            | <b>100%</b>          | <b>\$ 72,630</b>                            | <b>100%</b>          | <b>\$ 3,927</b> | <b>5%</b>  |

Wholesale: Wholesale net revenue increased \$5.3 million or 12.2% to \$48.9 million for the three months ended June 30, 2008 from \$43.5 million for the three months ended June 30, 2007. The strengthening of the foreign currencies against the USD accounted for a \$2.1 million increase to revenue and which reflects changes in the exchange rates for the three months ended June 30, 2008 as compared to the three months ended June 30, 2007. The remaining increase occurred due to an increase in the wholesale business in the United States, United Kingdom and Italy.

The following table reflects net revenue for each major country (in thousands, except percentages):

Wholesale Revenue by Country in USD

|                | For the Three Months Ended<br>June 30, 2008 |                         | For the Three Months Ended<br>June 30, 2007 |                         | Year-over-Year  |            |
|----------------|---|-------------------------|---|-------------------------|-----------------|------------|
|                | Net<br>Revenue                              | % of<br>Total Wholesale | Net<br>Revenue                              | % of<br>Total Wholesale | Variance        | Variance % |
| United States  | \$ 20,060                                   | 41%                     | \$ 16,055                                   | 37%                     | \$ 4,005        | 25%        |
| United Kingdom | 15,418                                      | 32%                     | 13,488                                      | 31%                     | 1,930           | 14%        |
| Germany        | 4,839                                       | 10%                     | 5,200                                       | 12%                     | (361)           | (7)%       |
| Spain          | 1,906                                       | 4%                      | 3,153                                       | 7%                      | (1,247)         | (40)%      |
| Italy          | 5,068                                       | 10%                     | 3,271                                       | 8%                      | 1,797           | 55%        |
| Other          | 1,575                                       | 3%                      | 2,350                                       | 5%                      | (775)           | (33)%      |
| <b>Total</b>   | <b>\$ 48,866</b>                            | <b>100%</b>             | <b>\$ 43,517</b>                            | <b>100%</b>             | <b>\$ 5,349</b> | <b>12%</b> |

Cost of revenue increased \$1.1 million to \$142.7 million, or 60.4% of net revenue, for the three months ended June 30, 2008 from \$141.6 million, or 62.6% of net revenue, for the three months ended June 30, 2007. We continue to grow revenue from our higher margin services and improve the cost efficiency of our network. We also received a benefit of \$5.8 million in Australia from the 2008 ACCC Ruling which reduced our cost of revenue and more than offset the increase experienced in line with the revenue growth.

United States: United States cost of revenue increased \$0.8 million or 6.8% to \$12.9 million for the three months ended June 30, 2008 from \$12.1 million for the three months ended June 30, 2007. The increase is primarily due to an increase of \$1.4 million in retail VOIP, which is partially offset by a \$0.5 million decrease in retail voice services.

Canada: Canada cost of revenue increased \$1.2 million or 4.3% to \$29.3 million for the three months ended June 30, 2008 from \$28.1 million for the three months ended June 30, 2007. This increase in cost is due to an increase of \$2.3 million in Internet services, \$0.5 million increases in prepaid services and a \$0.3 million increase in local services. The strengthening of the CAD against the USD accounted for a \$2.5 million increase to cost of revenue, which reflects changes in the exchange rates for the three months ended June 30, 2008 as compared to the three months ended June 30, 2007.





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Europe: European cost of revenue decreased by \$0.7 million primarily due to a decrease of \$1.5 million in net revenue.

Asia-Pacific: Asia-Pacific cost of revenue decreased \$5.3 million primarily due to a \$5.8 million reduction to cost of revenue from the 2008 ACCC Ruling. The strengthening of the AUD against the USD accounted for a \$6.3 million increase to cost of revenue, which is included in the explanations above, and which reflects changes in the exchange rates for the three months ended June 30, 2008 as compared to the three months ended June 30, 2007.

Wholesale: Wholesale cost of revenue increased \$5.1 million or 12.0% to \$47.2 million for the three months ended June 30, 2008 from \$42.2 million for the three months ended June 30, 2007 in line with the revenue increase. The strengthening of the foreign currencies against the USD accounted for a \$2.1 million increase to cost of revenue, which is included in the above variance, and which reflects changes in the exchange rates for the three months ended June 30, 2008 as compared to the three months ended June 30, 2007.

*Selling, general and administrative expenses* increased \$1.7 million to \$70.2 million, or 29.7% of net revenue, for the three months ended June 30, 2008 from \$68.5 million, or 30.3% of net revenue, for the three months ended June 30, 2007. The increase in selling, general and administrative expenses is attributable to an increase of \$3.3 million in salaries and benefits for additional sales and sales support personnel, an increase of \$1.0 million in advertising expenses, and an increase of \$0.3 million in occupancy expenses. These increases were partially offset by a decrease of \$2.1 million in professional fees because of fees for litigation defense and the FIN No. 48 Implementation, and a decrease of \$1.0 million in general and administrative expenses.

United States: United States selling, general and administrative expenses decreased \$2.1 million to \$13.5 million for three months ended June 30, 2008 from \$15.6 million for the three months ended June 30, 2007. The decrease is attributable to a decrease of \$1.6 million in professional fees attributable to a drop in legal fees for litigation, a decrease of \$0.4 million in salaries and benefits, and a decrease of \$0.4 million in general and administrative expenses. These decreases were offset by an increase of \$0.7 million in advertising expenses.

Canada: Canada selling, general and administrative expense increased \$1.8 million to \$25.1 million for the three months ended June 30, 2008 from \$23.3 million for three months ended June 30, 2007. The increase is attributable to an increase of \$1.6 million in salaries and benefits and an increase of \$1.2 million in sales and marketing. These increases were partially offset by a decrease of \$0.7 million in advertising expense and a decrease of \$0.6 million in general and administrative expenses.

Europe: Europe selling, general and administrative expense decreased \$1.5 million to \$6.4 million for the three months ended June 30, 2008 from \$7.8 million for the three months ended June 30, 2007. The decrease is attributable to a decrease of \$0.7 million in sales and marketing expenses, a decrease of \$0.3 million in occupancy expenses, and a decrease of \$0.5 million in general and administrative expenses.

Asia-Pacific: Asia-Pacific selling, general and administrative expense increased \$3.6 million to \$23.2 million for the three months ended June 30, 2008 from \$19.5 million for the three months ended June 30, 2007. The increase is attributable to an increase of \$2.2 million in salaries and benefits expenses, an increase of \$0.9 million in advertising expenses, an increase of \$0.5 million in general and administrative expenses, and an increase of \$0.5 million in occupancy expenses.

Wholesale: Wholesale selling, general and administrative expense decreased \$0.1 million or 5.5% to \$2.2 million for the three months ended June 30, 2008 from \$2.3 million for the three months ended June 30, 2007.

*Depreciation and amortization expense* increased \$0.8 million to \$8.1 million for the three months ended June 30, 2008 from \$7.3 million for the three months ended June 30, 2007. The increase consists of an increase in depreciation expense of \$1.2 million for assets placed in service as we enhanced our network infrastructure and expanded our data centers.

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*(Gain) loss on sale or disposal of assets* decreased by \$0.6 million to \$0.1 million for the three months ended June 30, 2008 as compared to \$0.7 million for the three months ended June 30, 2007.

*Interest expense and accretion on debt premium (discount), net* decreased \$3.2 million to \$13.3 million for the three months ended June 30, 2008 from \$16.5 million for the three months ended June 30, 2007. The decrease is mainly resulting from our debt restructuring activities.

*Gain (loss) on early extinguishment or restructuring of debt* was a \$32.3 million gain for the three months ended June 30, 2008 as compared to a \$2.3 million loss for the three months ended June 30, 2007. In the second quarter 2008, the Company exchanged \$49.0 million principal amount of the Company's 8% Senior Notes, \$33.0 million principal amount of the Company's 5% Exchangeable Senior Notes, \$43.1 million principal amount of the Company's 3 1/4% Convertible Senior Notes, \$5.3 million principal amount of the Company's 1 1/4% Senior Notes, and \$4.7 million of cash for \$67.1 million principal amount of newly issued 14 1/4% Senior Secured Notes of the Company and \$4.7 million of cash resulting in a gain on restructuring of debt of \$32.2 million including the expensing of related financing costs.

*Foreign currency transaction gain* was \$8.2 million for the three months ended June 30, 2008 as compared to \$15.1 million for the three months ended June 30, 2007. These gains are attributable to the impact of foreign currency exchange rate changes on intercompany debt balances and on receivables and payables denominated in a currency other than the subsidiaries' functional currency.

*Income tax benefit* was \$2.4 million benefit for the three months ended June 30, 2008 as compared to \$6.7 million benefit for the three months ended June 30, 2007. The benefit consists of a favorable final settlement of Canadian audits for the years 2000, 2001 and 2002, which resulted in a release of a FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes, liability of \$3.2 million, partially offset by foreign withholding tax on intercompany interest and royalty fees owed to a United States subsidiary by our Canadian and Australian subsidiaries.

*Results of operations for the six months ended June 30, 2008 as compared to the six months ended June 30, 2007*

*Net revenue* increased \$10.1 million or 2.2% to \$462.5 million for the six months ended June 30, 2008 from \$452.4 million for the six months ended June 30, 2007. Our revenue from broadband, VOIP, local, wireless, data and hosting services contributed \$121.8 million for the six months ended June 30, 2008, as compared to \$103.3 million for the six months ended June 30, 2007. Our wholesale carrier and prepaid services contributed \$90.7 million and \$19.6 million, respectively, for the six months ended June 30, 2008, as compared to \$88.5 million and \$25.0 million, respectively, for the six months ended June 30, 2007.

United States: United States retail net revenue decreased \$5.3 million or 9.6% to \$50.4 million for the six months ended June 30, 2008 from \$55.7 million for the six months ended June 30, 2007. The decrease is primarily attributed to a decrease of \$7.1 million in retail voice services (for residential and small businesses) and a decrease of \$0.7 million in Internet services, partially offset by an increase of \$2.5 million in retail VOIP.

Canada: Canada retail net revenue increased \$11.2 million or 8.9% to \$137.4 million for the six months ended June 30, 2008 from \$126.2 million for the six months ended June 30, 2007. The increase is primarily attributed to an increase of \$8.3 million in Internet, data and hosting services, an increase of \$4.5 million in local service, an increase of \$1.0 million in VOIP services and an increase of \$0.6 million in wireless services. These increases were partially offset by decreases of \$2.2 million in prepaid services and \$0.9 million in voice services. The strengthening of the CAD against the USD accounted for a \$16.1 million increase to revenue, which is included in the explanations above, and which reflects changes in the exchange rates for the six months ended June 30, 2008 as compared to the six months ended June 30, 2007.

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The following table reflects net revenue for each major country in North America (in thousands, except percentages):

Revenue by Country (Excluding Wholesale) in USD

|               | For the Six Months Ended |               | Year-over-Year |            |
|---------------|--------------------------|---------------|----------------|------------|
|               | June 30, 2008            | June 30, 2007 | Variance       | Variance % |
|               | Net Revenue              | Net Revenue   |                |            |
| United States | \$ 45,578                | \$ 53,079     | \$ (7,501)     | (14)%      |
| Canada        | \$ 137,438               | \$ 126,160    | \$ 11,278      | 9%         |
| Other         | \$ 4,837                 | \$ 2,666      | \$ 2,171       | 81%        |

Europe: European retail net revenue decreased \$5.8 million or 15.0% to \$32.7 million for the six months ended June 30, 2008 from \$38.5 million for the six months ended June 30, 2007. The decrease is primarily attributable to a \$1.5 million decrease in low margin prepaid services, a \$4.4 million decrease in retail voice services and a \$0.9 million decrease in wireless services. These decreases were partially offset by an increase of \$1.1 million in VOIP services. The strengthening of the European currencies against the USD accounted for a \$2.7 million increase to revenue, which is included in the explanations above, when comparing the exchange rates for the six months ended June 30, 2008 as compared to the six months ended June 30, 2007. The following table reflects net revenue for each major country in Europe (in thousands, except percentages):

Revenue by Country (Excluding Wholesale) in USD

|                | For the Six Months Ended |               | For the Six Months Ended |               | Year-over-Year |            |
|----------------|--------------------------|---------------|--------------------------|---------------|----------------|------------|
|                | June 30, 2008            | June 30, 2007 | June 30, 2008            | June 30, 2007 | Variance       | Variance % |
|                | Net Revenue              | % of Europe   | Net Revenue              | % of Europe   |                |            |
| United Kingdom | \$ 13,600                | 42%           | \$ 23,762                | 62%           | \$ (10,162)    | (43)%      |
| France         | 8,953                    | 27%           | 4,614                    | 12%           | 4,339          | 94%        |
| Belgium        | 4,283                    | 13%           | 4,839                    | 13%           | (556)          | (11)%      |
| Spain          | 2,312                    | 7%            | 2,749                    | 7%            | (437)          | (16)%      |
| Other          | 3,542                    | 11%           | 2,508                    | 6%            | 1,034          | 41%        |
| Europe Total   | \$ 32,690                | 100%          | \$ 38,472                | 100%          | \$ (5,782)     | (15)%      |

Asia-Pacific: Asia-Pacific net revenue increased \$7.7 million or 5.4% to \$151.3 million for the six months ended June 30, 2008 from \$143.6 million for the six months ended June 30, 2007. The increase is primarily attributable to a \$3.9 million increase in Australia DSL services, a \$5.8 million increase in Australia business and residential voice services, and a \$0.7 million increase in wireless services, partially offset by a \$2.0 million decrease in dial-up Internet services. The strengthening of the AUD against the USD accounted for a \$20.5 million increase to revenue, which is included in the explanations above, which reflects changes in the exchange rates for the six months ended June 30, 2008 as compared to the six months ended June 30, 2007. The following table reflects net revenue for each major country in Asia-Pacific (in thousands, except percentages):

Revenue by Country (Excluding Wholesale) in USD

|           | For the Six Months Ended |                   | For the Six Months Ended |                   | Year-over-Year |            |
|-----------|--------------------------|-------------------|--------------------------|-------------------|----------------|------------|
|           | June 30, 2008            | June 30, 2007     | June 30, 2008            | June 30, 2007     | Variance       | Variance % |
|           | Net Revenue              | % of Asia-Pacific | Net Revenue              | % of Asia-Pacific |                |            |
| Australia | \$ 150,066               | 99%               | \$ 142,151               | 99%               | \$ 7,915       | 6%         |
| Other     | 1,212                    | 1%                | 1,401                    | 1%                | (189)          | (13)%      |

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|                    |            |      |            |      |          |    |
|--------------------|------------|------|------------|------|----------|----|
| Asia-Pacific Total | \$ 151,278 | 100% | \$ 143,552 | 100% | \$ 7,726 | 5% |
|--------------------|------------|------|------------|------|----------|----|

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Wholesale: Wholesale net revenue increased \$2.2 million or 2.5% to \$90.7 million for the six months ended June 30, 2008 from \$88.5 million for the six months ended June 30, 2007. The strengthening of the foreign currencies against the USD accounted for a \$4.1 million increase to revenue, which is included in the above explanation, and which reflects changes in the exchange rates for the six months ended June 30, 2008 as compared to the six months ended June 30, 2007. The following table reflects net revenue for each major country (in thousands, except percentages):

## Wholesale Revenue by Country in USD

|                | For the Six Months Ended<br>June 30, 2008 |                         | For the Six Months Ended<br>June 30, 2007 |                         | Year-over-Year    |            |
|----------------|---|-------------------------|---|-------------------------|-------------------|------------|
|                | Net Revenue                               | % of<br>Total Wholesale | Net Revenue                               | % of<br>Total Wholesale | Variance          | Variance % |
| United States  | \$ 39,586                                 | 44%                     | \$ 35,676                                 | 40%                     | \$ 3,910          | 11%        |
| United Kingdom | 25,981                                    | 29%                     | 26,211                                    | 30%                     | (230)             | (1)%       |
| Germany        | 9,748                                     | 11%                     | 10,116                                    | 11%                     | (368)             | (4)%       |
| Spain          | 4,013                                     | 4%                      | 5,426                                     | 6%                      | (1,413)           | (26)%      |
| Italy          | 7,851                                     | 9%                      | 6,130                                     | 7%                      | 1,721             | 28%        |
| Other          | 3,542                                     | 3%                      | 4,945                                     | 6%                      | (1,403)           | (28)%      |
| <b>Total</b>   | <b>\$ 90,721</b>                          | <b>100%</b>             | <b>\$ 88,504</b>                          | <b>100%</b>             | <b>\$ (2,217)</b> | <b>3%</b>  |

*Cost of revenue* decreased \$1.1 million to \$284.5 million, or 61.5% of net revenue, for the six months ended June 30, 2008 from \$285.7 million, or 63.1% of net revenue, for the six months ended June 30, 2007. We continue to grow revenue from our higher margin services and improve the cost efficiency of our network. We also received a benefit of \$5.8 million in Australia from the 2008 ACCC Ruling which reduced our cost of revenue and more than offset the increase experienced in line with the revenue growth.

United States: United States cost of revenue decreased \$0.1 million primarily due to a decrease of \$1.4 million in retail revenue, offset by an increase of \$1.4 million in VOIP services.

Canada: Canada cost of revenue increased \$2.4 million primarily due to an increase of \$7.3 million from the strengthening of the CAD against the USD which reflects changes in the exchange rates for the six months ended June 30, 2008 as compared to the six months ended June 30, 2007, offset by declines in line with changes in revenue.

Europe: European cost of revenue decreased by \$2.3 million primarily due to a decrease of \$5.8 million in net revenue.

Asia-Pacific: Asia-Pacific cost of revenue decreased \$3.2 million primarily due to a decrease of \$2.3 million in residential business and a decrease of \$1.3 million in Internet services. We also realized a \$5.8 million reduction to cost of revenue from the 2008 ACCC Ruling. These decreases were partially offset by an increase of \$3.2 million in business services and an increase of \$1.9 million in Australian DSL services. The strengthening of the AUD against the USD accounted for a \$13.2 million increase to cost of revenue, which is included in the explanations above, and which reflects changes in the exchange rates for the six months ended June 30, 2008 as compared to the six months ended June 30, 2007.

Wholesale: Wholesale cost of revenue increased \$2.1 million or 2.5% to \$87.7 million for the six months ended June 30, 2008 from \$85.6 million for the six months ended June 30, 2007 in line with the revenue increase. The strengthening of the foreign currencies against the USD accounted for a \$4.0 million increase to cost of revenue, which is included in the above variance explanation, and which reflects changes in the exchange rates for the six months ended June 30, 2008 as compared to the six months ended June 30, 2007.

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*Selling, general and administrative expenses* increased \$3.2 million to \$139.4 million, or 30.1% of net revenue, for the six months ended June 30, 2008 from \$136.2 million, or 30.1% of net revenue, for the six months ended June 30, 2007. The increase in selling, general and administrative expenses is attributable to an increase of \$5.8 million in salaries and benefits, an increase of \$1.3 million in sales and marketing expenses, an increase of \$1.1 million in advertising, and an increase of \$1.6 million in occupancy expenses. These increases were partially offset by a decrease of \$5.4 million in professional fees (described below) and a decrease of \$1.6 million in general and administrative expenses.

United States: United States selling, general and administrative expenses decreased \$4.6 million to \$26.5 million for six months ended June 30, 2008 from \$31.0 million for the six months ended June 30, 2007. The decrease is attributable to a decrease of \$4.1 million in professional fees as the first quarter 2007 included significant expenses for litigation defense and the FIN No. 48 implementation.

Canada: Canada selling, general and administrative expense increased \$3.1 million due to the strengthening of the CAD, accounting for a \$6.0 million increase to selling, general and administrative expense. This increase was offset by declines in advertising and general and administrative expenses.

Europe: Europe selling, general and administrative expense decreased \$3.2 million to \$12.1 million for the six months ended June 30, 2008 from \$15.3 million for the six months ended June 30, 2007. The decrease is attributable to a decrease of \$1.7 million in sales and marketing expense primarily in prepaid services agent commissions, a decrease of \$0.4 million in salaries and benefits, a decrease of \$0.6 million in occupancy expenses, and a decrease of \$0.4 million in general and administrative services.

Asia-Pacific: Asia-Pacific selling, general and administrative expense increased \$8.0 million due to the strengthening of the AUD, accounting for a \$5.5 million increase to selling, general and administrative expense and increases in sales and marketing, advertising and occupancy expenses.

Wholesale: Wholesale selling, general and administrative expense decreased \$0.1 million or 1.6% to \$4.2 million for the six months ended June 30, 2008 from \$4.3 million for the six months ended June 30, 2007.

*Depreciation and amortization expense* increased \$2.2 million to \$16.1 million for the six months ended June 30, 2008 from \$13.9 million for the six months ended June 30, 2007. The increase consists of an increase in depreciation expense of \$2.6 million for assets placed in service as we enhanced our network infrastructure and expanded our data centers.

*(Gain) loss on sale or disposal of assets* was a \$2.5 million gain for the six months ended June 30, 2008 compared to a \$0.7 million loss for the six months ended June 30, 2007. In the six months ended June 30, 2008, we recognized a gain of \$0.8 million associated with the sale of certain surplus fiber assets in the US and a gain of \$1.8 million associated with a sale of a minority equity investment in a Japanese entity.

*Interest expense and accretion on debt premium (discount), net* decreased \$1.7 million to \$28.6 million for the six months ended June 30, 2008 from \$30.2 million for the six months ended June 30, 2007. There was an increase of \$3.2 million mainly resulting from issuance and exchange of our 14<sup>1</sup>/<sub>4</sub>% Senior Secured Notes, offset by a \$4.8 million decrease mainly resulting from reductions in principal outstanding balances of our 12<sup>3</sup>/<sub>4</sub>% Senior Notes, Step Up Convertible Subordinated Debentures, 8% Senior Notes, 5% Exchangeable Senior Notes, and 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes.

*Gain (loss) on early extinguishment or restructuring of debt* was a \$34.5 million gain for the six months ended June 30, 2008 compared to an \$8.3 million loss for the six months ended June 30, 2007. In the second quarter 2008, we exchanged \$49.0 million principal amount of our 8% Senior Notes, \$33.0 million principal amount of our 5% Exchangeable Senior Notes, \$43.1 million principal amount of our 3<sup>3</sup>/<sub>4</sub>% Convertible Senior Notes, \$5.3 million principal amount of our 12<sup>3</sup>/<sub>4</sub>% Senior Notes for \$67.1 million principal amount of our newly

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issued 14 1/4% Senior Secured Notes and \$4.7 million of cash, resulting in a gain on restructuring of debt of \$32.2 million including the expensing of related financing costs. In the first quarter 2008, we made open market purchases of \$0.8 million principal amount of our October 1999 Senior Notes and \$13.8 million principal amount of our Step Up Convertible Subordinated Debentures, resulting in a \$0.1 million and \$2.1 million gain, respectively, on early extinguishment of debt including the write-off of related deferred financing costs, discount and effective interest.

In the second quarter 2007, we converted \$5.0 million principal amount of our Step Up Convertible Subordinate Debentures to 6.0 million shares of our common stock, resulting in an induced debt conversion expense of \$2.3 million, which includes deferred financing cost and discount write-offs. In first quarter 2007, we issued in a private transaction \$57.2 million principal amount of the 14 1/4% Senior Secured Notes in exchange for \$40.7 million principal amount of the Company's outstanding 12 1/4% Senior Notes and \$23.6 million in cash. This exchange was deemed a debt modification, resulting in a \$5.1 million loss on restructuring of debt for financing costs incurred. The remaining \$0.9 million of expense in the three months ended June 30, 2007, resulted from costs related to the early retirement of a Canadian credit facility.

*Foreign currency transaction gain* was \$9.8 million for the six months ended June 30, 2008 as compared to \$18.1 million for the six months ended June 30, 2007. These gains are attributable to the impact of foreign currency exchange rate changes on intercompany debt balances and on receivables and payables denominated in a currency other than the subsidiaries' functional currency.

*Income tax benefit (expense)* was an expense of \$37 thousand for the six months ended June 30, 2008 as compared to \$5.7 million benefit for the six months ended June 30, 2007. The six months ended June 30, 2008 amount consists of a favorable final settlement of Canadian audits for the years 2000, 2001 and 2002, which resulted in a release of a FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes, liability of \$3.2 million, offset by foreign withholding tax on intercompany interest and royalty fees owed to a United States subsidiary by our Canadian and Australian subsidiaries.

**Liquidity and Capital Resources*****Changes in Cash Flows***

Our principal liquidity requirements arise from cash used in operating activities, purchases of network equipment including switches, related transmission equipment and capacity, development of back-office systems, expansion of data center facilities, interest and principal payments on outstanding debt and other obligations, repurchase and retirement of debt obligations, taxes and acquisitions. We have financed our growth and operations to date through public offerings and private placements of debt and equity securities, vendor financing, capital lease financing and other financing arrangements.

Net cash provided by operating activities was \$5.3 million for both six months periods ended June 30, 2008 and 2007. For the six months ended June 30, 2008, net income, net of non-cash operating activity, provided \$21.5 million of cash. In addition, cash was increased by a reduction in prepaid expenses, other current assets and other assets of \$12.1 million and an increase in accrued interconnection costs of \$3.2 million. For the six months ended June 30, 2008, we used \$6.4 million to increase our accounts receivable, \$16.6 million to reduce our accounts payable, \$0.9 million to reduce our accrued interest, \$4.5 million to reduce our accrued income taxes and \$3.1 million to reduce our accrued expenses, deferred revenue, other current liabilities and other liabilities. For the six months ended June 30, 2007, net income, net of non-cash operating activity, provided \$12.5 million of cash. In addition, cash was increased by a reduction in accounts receivable of \$1.0 million, a reduction in prepaid expenses and other current assets of \$2.1 million and an increase in our deferred revenue, accrued expenses, and other liabilities of \$0.9 million. In 2007, we used \$5.2 million to reduce our accounts payable and accrued interconnection costs, \$4.8 million to reduce our accrued income taxes and \$1.0 million to reduce our accrued interest.

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Net cash used in investing activities was \$12.0 million for the six months ended June 30, 2008 compared to \$10.9 million for the six months ended June 30, 2007. Net cash used in investing activities during the six months ended June 30, 2008 included \$14.6 million of capital expenditures offset by \$1.7 million net cash proceeds from the disposition of a minority equity investment in Japan and \$0.8 million from the disposition of surplus fiber assets. Net cash used in investing activities during the six months ended June 30, 2007 included \$17.0 million of capital expenditures, offset by \$5.5 million net cash proceeds from the disposition of our Australian Planet Domain business operations.

Net cash used in financing activities was \$19.5 million for the six months ended June 30, 2008 as compared to \$44.5 million provided by financing activities for the six months ended June 30, 2007. During the six months ended June 30, 2008, \$11.2 million was used to purchase and retire \$0.8 million principal amount of our 12<sup>3/4</sup>% Senior Notes and \$13.8 million principal amount of our Step Up Convertible Subordinated Debentures. We also used \$8.3 million for debt exchanges and principal payments on capital leases, leased fiber capacity, financing facilities and other long-term obligations. During the six months ended June 30, 2007, net cash provided by financing activities consisted of \$102.7 million from the issuance of \$75.2 million principal amount of 14<sup>1/4</sup> % Senior Secured Notes for \$69.2 million in cash and the issuance of \$33.5 million through a credit facility with a financial institution, net of \$1.5 million in financing costs; partially offset by the retirement in full of the \$22.7 million principal amount of our 2000 Convertible Subordinated Debentures, the repayment in full of a \$29.9 million Canadian loan facility and \$5.6 million principal payments of capital leases, leased fiber capacity, financing facilities and other long-term obligations.

### ***Short- and Long-Term Liquidity Considerations and Risks***

As of June 30, 2008, we had \$55.6 million of cash and cash equivalents. We believe that our existing cash and cash equivalents, will be sufficient to fund our debt service requirements, other fixed obligations (such as capital leases, vendor financing and other long-term obligations), and other cash needs for our operations for at least the next twelve months. Our strategies related to meeting our 2009 obligations and other cash needs are to strengthen the balance sheet opportunistically through potential de-leveraging transactions and equity capital infusions; to improve the non-sales and marketing cost structure and maintain an aggressive cost management program; to focus on improving sales productivity and margin enhancements by leveraging the network assets and increasing the revenue mix in favor of higher margin growth services; and opportunistically to sell non-strategic assets and businesses and use the proceeds either to accelerate increases in high margin products or to reduce debt.

During 2007 and the first half of 2008 we successfully executed a number of liquidity-enhancing initiatives. As a result of these transactions, we have \$14.2 million principal amount of 12<sup>3/4</sup> % Senior Notes and \$8.6 million principal amount of Step Up Convertible Subordinated Debentures coming due in the second half of 2009. We have extended our debt maturities, reduced the principal amount of debt maturing in 2009 and 2010, and have added financial flexibility, subject to the limitations noted below, to make additional investments in our higher margin growth businesses. Broadband, VOIP, local, wireless, data and hosting services are generating a second quarter 2008 annualized revenue run-rate of \$247 million. Exploiting the full potential for these services will require a greater investment in sales and marketing over the next year. Such an investment seems justified given our need for revenue and profitability growth from these services to compensate for the corresponding declines from our legacy long distance voice and dial-up Internet businesses. We expect overall revenue to show a slight increase in 2008 as compared to 2007. Our challenge is to have contribution from these growth products continue to eclipse the decline in our legacy businesses beyond that which we executed in the first six months of 2008.



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As of June 30, 2008, we had \$19.0 million in future minimum purchase obligations, \$56.2 million in future operating lease payments and \$618.2 million of indebtedness. As of June 30, 2008, approximately \$104.0 million of unrecognized tax benefits have been recorded in accordance with FIN No. 48. We are uncertain as to if or when such amounts may be settled due to the unpredictable nature and timing of income tax audits, so we have not included these amounts in the table below. Payments of principal and interest are due as follows:

| Year Ending December 31,  | Vendor Financing | Senior Secured Term Loan Facility (1) | Financing Facility | Senior Notes      | Convertible and Exchangeable Notes (2) | Step Up Convertible Subordinated Debentures | Senior Secured Notes (2) | Purchase Obligations | Operating Leases | Total             |
|---|------------------|---------------------------------------|--------------------|-------------------|--|---|--------------------------|----------------------|------------------|-------------------|
| (amounts in thousands)  |                  |                                       |                    |                   |  |   |                          |                      |                  |                   |
| 2008 (as of June 30, 2008)  | \$ 5,477         | \$ 5,234                              | \$ 1,562           | \$ 8,344          | \$ 1,225                               | \$ 346                                      | \$ 13,486                | \$ 4,051             | \$ 7,960         | \$ 47,685         |
| 2009  | 3,550            | 10,396                                | 3,124              | 30,875            | 2,451                                  | 9,332                                       | 24,980                   | 7,503                | 13,089           | 105,300           |
| 2010  | 3,327            | 10,298                                | 3,124              | 14,880            | 59,436                                 |   | 24,980                   | 3,316                | 10,018           | 129,379           |
| 2011  | 75               | 94,250                                | 3,124              | 14,880            |  |   | 186,789                  | 2,584                | 7,288            | 308,990           |
| 2012  | 44               |                                       | 35,781             | 14,880            |  |   |                          | 1,587                | 5,692            | 57,984            |
| Thereafter  | 62               |                                       | 0                  | 208,320           |  |   |                          |                      | 12,174           | 220,556           |
| <b>Total Minimum Principal &amp; Interest Payments</b>  | <b>12,535</b>    | <b>120,178</b>                        | <b>46,715</b>      | <b>292,179</b>    | <b>63,112</b>                          | <b>9,678</b>                                | <b>250,235</b>           | <b>19,041</b>        | <b>56,221</b>    | <b>869,894</b>    |
| Less: Amount Representing Interest  | (999)            | (23,428)                              | (11,715)           | (91,993)          | (5,543)                                | (1,037)                                     | (74,934)                 |                      |                  | (209,649)         |
| <b>Face Value of Long-term Obligations</b>  | <b>11,536</b>    | <b>96,750</b>                         | <b>35,000</b>      | <b>200,186</b>    | <b>57,569</b>                          | <b>8,641</b>                                | <b>175,301</b>           | <b>19,041</b>        | <b>56,221</b>    | <b>660,245</b>    |
| Amount Representing Premium (Discount)  |                  |                                       |                    |                   | (246)                                  | (340)                                       | 5,038                    |                      |                  | 4,452             |
| <b>Add: Exchangeable Notes and Senior Secured Notes Interest Treated as Long-Term Obligations</b> |                  |                                       |                    |                   | <b>2,337</b>                           |   | <b>26,405</b>            |                      |                  | <b>28,742</b>     |
| <b>Total Long-Term Obligation</b>   | <b>\$ 11,536</b> | <b>\$ 96,750</b>                      | <b>\$ 35,000</b>   | <b>\$ 200,186</b> | <b>\$ 59,660</b>                       | <b>\$ 8,301</b>                             | <b>\$ 206,744</b>        | <b>\$ 19,041</b>     | <b>\$ 56,221</b> | <b>\$ 693,439</b> |

- (1) For preparation of this table, we have assumed the interest rate of the Senior Secured Term Loan Facility to be 9.8%, which is the interest rate at June 30, 2008.
- (2) For preparation of this table, we have shown separately the cash interest payments of the 5% Exchangeable Senior Notes and these 14 1/4 % Senior Secured Notes that were issued through trouble debt restructurings as a portion of long-term obligations (see *Senior Notes, Senior Secured Notes, Convertible Senior Notes, Exchangeable Senior Notes, Step Up Convertible Subordinated Debentures and Convertible Subordinated Debentures* below). The interest due on the 5% Exchangeable Senior Notes in 2008, 2009 and 2010 is \$0.6 million, \$1.2 million and \$0.6 million, respectively. The interest due on this portion of the 14 1/4 % Senior Secured Notes in 2008, 2009, 2010 and 2011 is \$5.4 million, \$8.8 million, \$8.8 million and \$3.4 million, respectively.
- We have contractual obligations to utilize network facilities from certain carriers with terms greater than one year. We generally do not purchase or commit to purchase quantities in excess of normal usage or amounts that cannot be used within the contract term. We have minimum annual purchase obligations of \$4.1 million, \$7.5 million, \$3.3 million, \$2.6 million and \$1.6 million remaining in 2008, 2009, 2010, 2011 and 2012, respectively.

The indentures governing the senior notes, convertible senior notes, exchangeable senior notes, step up convertible subordinated debentures, senior secured notes and the senior secured term loan facility, as well as other credit arrangements, contain certain financial and other covenants which, among other things, will restrict our ability to incur further indebtedness and make certain payments, including the payment of dividends and repurchase of subordinated debt and certain debt issued by us. We were in compliance with the above covenants at June 30, 2008.

We will continue to have significant debt service obligations on a long-term basis. From time to time, we consider the feasibility and timing of transactions that could raise capital for additional liquidity, debt reduction, refinancing of existing indebtedness and for additional working

capital and growth opportunities. There can be no assurance we will be successful

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in any of these efforts to obtain any such financing on acceptable terms or at all. If we are successful in raising additional financing or issuing our securities in exchange for debt, securities comprising a significant percentage of our diluted equity capital may be issued in connection with the completion of such transactions. Additionally, if our plans or assumptions change or prove inaccurate, including those with respect to our debt levels, competitive developments, developments affecting our network or product initiatives, services, operations or cash from operating activities, if we consummate additional investments or acquisitions, if we experience unexpected costs or competitive pressures or if existing cash and any other borrowings prove to be insufficient, we may need to obtain such financing and/or relief sooner than expected. In such circumstances, there can be no assurance we will be successful in these efforts to obtain new capital at acceptable terms. Also there can be no assurance that changes in assumptions or conditions, including those referenced under Risk Factors, Legal Proceedings and Special Note Regarding Forward-Looking Statements will not adversely affect our financial condition or short-term or long-term liquidity.

In light of the foregoing, we and/or our subsidiaries will evaluate and determine on a continuing basis, depending on market conditions and the outcome of events described herein under Special Note Regarding Forward Looking Statements, the most efficient use of our capital and resources, including investment in our network, systems and growth products, purchasing, refinancing, exchanging, tendering for or retiring certain of our outstanding debt securities in privately negotiated transactions, open market transactions or by other direct or indirect means, issuing our common stock or purchasing our common stock in the open market to the extent permitted by existing covenants.

## **New Accounting Pronouncements**

In March 2008, the Financial Accounting Standard Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 161, Disclosures about Derivative Instruments and Hedging Activities. SFAS No. 161 amends and expands the disclosure requirements of SFAS No. 133, Accounting for Derivative Instruments and Hedging with the intent to provide users of financial statements with an enhanced understanding of use of derivative instruments, how derivative instruments and related hedged items are accounted for, and how derivative instruments and related hedged items affect an entity's financial statements. SFAS No. 161 is effective for financial statements issued for fiscal years after July 1, 2009. We anticipate that the adoption of this standard will not have a material impact on our results of operations, financial position and cash flows.

## **Special Note Regarding Forward Looking Statements**

Certain statements in this Quarterly Report on Form 10-Q and elsewhere constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Such statements are based on current expectations, and are not strictly historical statements. Forward-looking statements include, without limitation, statements set forth in this document and elsewhere regarding, among other things:

expectations of future growth, creation of shareholder value, revenue, foreign revenue contributions and net income, as well as income from operations, margins, earnings per share, cash flow and cash sufficiency levels, working capital, network development, customer migration and related costs, spending on and success with growth products, including broadband Internet, VOIP, wireless, local, data and hosting services, traffic development, capital expenditures, selling, general and administrative expenses, income tax and withholding tax expense, fixed asset and goodwill impairment charges, service introductions, cash requirements and potential asset sales;

increased competitive pressures, declining usage patterns, and our growth products, bundled service offerings, the pace and cost of customer migration onto our networks, the effectiveness and profitability of the growth products;

financing, refinancing, de-leveraging and/or debt repurchase, restructuring, exchange or tender plans or initiatives, and potential dilution of existing equity holders from such initiatives;

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liquidity and debt service forecast;

assumptions regarding currency exchange rates;

timing, extent and effectiveness of cost reduction initiatives and management's ability to moderate or control discretionary spending;

management's plans, goals, expectations, guidance, objectives, strategies, and timing for future operations, acquisitions, asset dispositions, product plans, performance and results;

management's assessment of market factors and competitive developments, including pricing actions and regulatory rulings; and

ability to generate net cash proceeds from the disposition of selective assets without material impairment to profitability.

Factors and risks that could cause actual results or circumstances to differ materially from those set forth or contemplated in forward looking statements include those set forth in Risk Factors as well as, without limitation:

changes in business conditions causing changes in the business direction and strategy by management;

heightened competitive pricing and bundling pressures in the markets in which we operate;

accelerated decrease in minutes of use on wireline phones;

fluctuations in the exchange rates of currencies, particularly of the USD relative to foreign currencies of the countries where we conduct our foreign operations;

adverse interest rate developments affecting our variable interest rate debt;

difficulty in maintaining or increasing customer revenues and margins through our product initiatives and bundled service offerings, and difficulties in migrating and provisioning broadband and local customers to DSL networks;

inadequate financial resources to promote and to market product initiatives;

fluctuations in prevailing trade credit terms or revenues due to the adverse impact of, among other things, further telecommunications carrier bankruptcies or adverse bankruptcy related developments affecting our large carrier customers;

the possible inability to raise additional capital when needed, on attractive terms, or at all;

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possible claims under our existing debt instruments which could impose constraints and limit our flexibility;

the inability to reduce, repurchase, refinance, exchange, tender for or restructure debt significantly, or in amounts sufficient to conduct regular ongoing operations;

the impact of the delisting of our common stock from the Nasdaq Capital Market which may impair our ability to raise capital;

further changes in the telecommunications or Internet industry, including rapid technological changes, regulatory and pricing changes in our principal markets and the nature and degree of competitive pressure that we may face;

adverse tax or regulatory rulings from applicable authorities;

enhanced broadband, DSL, Internet, wireless, VOIP, data and hosting and local and long distance voice telecommunications competition;

changes in financial, capital market and economic conditions;

changes in service offerings or business strategies, including the need to modify business models if performance is below expectations;

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difficulty in retaining existing long distance wireline and dial-up ISP customers;

difficulty in migrating or retaining customers associated with acquisitions of customer bases, or integrating other assets;

difficulty in selling new services in the marketplace;

difficulty in providing broadband, DSL, local, VOIP, data and hosting or wireless services;

changes in the regulatory schemes or requirements and regulatory enforcement in the markets in which we operate;

restrictions on our ability to execute certain strategies or complete certain transactions as a result of our inexperience with new products, or limitations imposed by available cash resources, our capital structure or debt covenants;

risks associated with our limited DSL, Internet, VOIP, data and hosting and wireless experience and expertise, including effectively utilizing new marketing channels such as interactive marketing employing the Internet;

entry into developing markets;

aggregate margin contribution from the new products is not sufficient in amount or timing to offset the margin decline in our legacy long distance voice and dial-up ISP businesses;

the possible inability to hire and/or retain qualified executive management, sales, technical and other personnel;

risks and costs associated with our effort to locate certain activities and functions off-shore;

risks associated with international operations;

dependence on effective information and billing systems;

possible claims for patent infringement on products or processes employed in providing our services;

dependence on third parties for access to their networks to enable us to expand and manage our global network and operations and to offer broadband, DSL, local, VOIP and wireless services, including dependence upon the cooperation of incumbent carriers relating to the migration of customers;

dependence on the performance of our global standard asynchronous transfer mode and Internet-based protocol (ATM+IP) communications network; risks associated with maintaining and upgrading networks;

adverse regulatory rulings or actions affecting our operations, including the imposition of taxes and fees, the imposition of obligations upon VOIP providers to provide enhanced 911 (E911) services and restricting access to broadband networks owned and operated by others, including the development of a national broadband network in Australia; and

the potential further elimination or limitation of a substantial amount or all of our United States or foreign operating loss carryforwards due to future significant issuances of equity securities, changes in ownership or other circumstances, which carryforwards would otherwise be available to reduce future taxable income.

As such, actual results or circumstances may vary materially from such forward looking statements or expectations. Readers are also cautioned not to place undue reliance on these forward looking statements which speak only as of the date these statements were made. We are not obligated to update or revise any forward looking statements, whether as a result of new information, future events or otherwise.

**Table of Contents****ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Our primary market risk exposures relate to changes in foreign currency exchange rates, valuations of derivatives and to changes in interest rates.

Foreign currency can have a major impact on our financial results. Currently in excess of 81% of our net revenue was derived from sales and operations outside the United States. The reporting currency for our consolidated financial statements is the USD. The local currency of each country is the functional currency for each of our respective entities operating in that country. In the future, we expect to continue to derive the majority of our net revenue and incur a significant portion of our operating costs from outside the United States, and therefore changes in exchange rates have had and may continue to have a significant, and potentially adverse, effect on our results of operations. Our primary risk of loss regarding foreign currency exchange rate risk is caused primarily by fluctuations in the following exchange rates: USD/CAD, USD/AUD, USD/GBP, and USD/EUR. Due to the large percentage of our revenue derived outside of the United States, changes in the USD relative to one or more of the foregoing currencies could have an adverse impact on our future results of operations. We have agreements with certain subsidiaries for repayment of a portion of the investments and advances made to these subsidiaries. As we anticipate repayment in the foreseeable future, we recognize the unrealized gains and losses in foreign currency transaction gain (loss) on the consolidated statements of operations. We historically have not engaged in hedging transactions. However, during the fourth quarter 2007, we completed a forward currency contract required by the Canadian Credit Agreement. The exposure of our income from operations to fluctuations in foreign currency exchange rates is reduced in part because a majority of the costs that we incur in connection with our foreign operations are also denominated in local currencies. Given the current divergence in exchange rates affecting the functional currencies in our major markets as compared to the USD, we will explore whether hedging activities may provide benefit to us.

We are exposed to financial statement gains and losses as a result of translating the operating results and financial position of our international subsidiaries. We translate the local currency statements of operations of our foreign subsidiaries into USD using the average exchange rate during the reporting period. Changes in foreign exchange rates affect the reported profits and losses and cash flows and may distort comparisons from year to year. By way of example, when the USD strengthens compared to the EUR, there could be a negative or positive effect on the reported results for Europe, depending upon whether Europe is operating profitably or at a loss. It takes more profits in EUR to generate the same amount of profits in USD and a greater loss in EUR to generate the same amount of loss in USD. The opposite is also true. For instance, when the USD weakens there is a positive effect on reported profits and a negative effect on reported losses for Europe.

In the three and six months ended June 30, 2008, as compared to the three and six months ended June 30, 2007, the USD was weaker on average as compared to the CAD, AUD, GBP and EUR. As a result, our revenue of the subsidiaries whose local currency is CAD, AUD, GBP and EUR decreased (0)%, (7)%, (15)% and (1)% in local currency compared to the three months ended June 30, 2007, but increased (decreased) 8%, 6%, (12)% and 15% in USD, respectively. Our revenue of the subsidiaries whose local currency is CAD, AUD, GBP and EUR decreased (4)%, (8)%, (25)% and (5)% in local currency compared to the six months ended June 30, 2007, but increased (decreased) 9%, 6%, (21)% and 9% in USD, respectively.

*Interest rates* The majority of our long-term debt obligations are at fixed interest rates at June 30, 2008. In February 2005, we obtained a \$100 million senior secured term loan, which has a variable interest rate feature. In March 2007, we entered into a \$35 million senior secured credit agreement with a variable interest rate. The interest rate on the \$35 million senior secured credit agreement has been fixed effective October 2007 after we completed a cross-currency interest rate swap agreement. We are exposed to interest rate risk as additional financing may be required. Our primary exposure to market risk stems from fluctuations in interest rates.

The interest rate sensitivity table below summarizes our market risks associated with fluctuations in interest rates for the six months ended June 30, 2008 in USD, which is our reporting currency. The table presents principal cash flows and related weighted average interest rates by year of expected maturity for our senior notes, senior secured notes, senior secured term loan, convertible senior notes, exchangeable senior notes, step up



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convertible subordinated debentures, leased fiber capacity, and other long-term obligations in effect at June 30, 2008. In the case of the convertible senior notes, exchangeable senior notes, step up convertible subordinated debentures and senior secured notes, the table excludes the potential exercise of the relevant redemption and conversion features and excludes an unamortized debt premium (net of discount) of \$4.5 million and future cash interest payments of \$28.7 million from our 5% Exchangeable Senior Notes and 14 1/4 % Senior Secured Note that are treated as long term obligations (see Note 4 – Long-Term Obligations ).

|                       | Year of Maturity                   |           |           |            |           |            | Total      | Fair Value |
|-----------------------|------------------------------------|-----------|-----------|------------|-----------|------------|------------|------------|
|                       | 2008                               | 2009      | 2010      | 2011       | 2012      | Thereafter |            |            |
|                       | (in thousands, except percentages) |           |           |            |           |            |            |            |
| Fixed Rate            | \$ 5,084                           | \$ 25,971 | \$ 60,711 | \$ 175,369 | \$ 35,041 | \$ 186,057 | \$ 488,233 | \$ 314,305 |
| Average Interest Rate | 9.6%                               | 10.7%     | 4.5%      | 14.2%      | 9.6%      | 8.0%       | 10.1%      |            |
| Variable Rate         | \$ 500                             | \$ 1,000  | \$ 1,000  | \$ 94,250  | \$        | \$         | \$ 96,750  | \$ 96,750  |
| Average Interest Rate | 9.8%                               | 9.8%      | 9.8%      | 9.8%       | 0.0%      | 0.0%       | 9.8%       |            |

**ITEM 4. CONTROLS AND PROCEDURES****Evaluation of Disclosure Controls and Procedures.**

Our management evaluated, with the participation of our Chief Executive Officer and Chief Financial Officer, the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report. Based on this evaluation, as a result of the material weakness described below, our principal executive officer and our principal financial officer have concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were not effective. Disclosure controls and procedures mean our controls and other procedures that are designed to ensure that information required to be disclosed by us in our reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by us in our reports that we file or submit under the Securities Exchange Act of 1934 is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosure.

As part of our compliance efforts relative to Section 404 of Sarbanes-Oxley Act of 2002, management assessed the effectiveness of internal control over financial reporting as of December 31, 2007. In making this assessment, management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission ( COSO ) in Internal Control-Integrated Framework. Based on the assessment, management identified a material weakness in our internal control over accounting for income taxes. The material weakness in internal control related to a lack of documentation and insufficient historical analysis, and has not been remediated because of insufficient time in the position for the Corporate Tax Director, who started in the position on October 1, 2007. His hiring was part of the remediation efforts related to the material weakness identified as December 31, 2006. This short time period did not allow the new Corporate Tax Director enough time to establish a consistent application of controls surrounding documentation and historical analysis. These deficiencies represent a material weakness in internal control over financial reporting on the basis that there is more than a remote likelihood that a material misstatement in our interim or annual financial statements due to errors in accounting for income taxes could occur and would not be prevented or detected by our internal control over financial reporting.

**Changes in Internal Control**

Our Principal Executive Officer and our Principal Financial Officer have concluded that there have been no changes in our internal control over financial reporting that occurred during the quarter ended June 30, 2008, that have materially affected, or is reasonably likely to affect materially, our internal control over financial reporting, except for the items noted below. We are in the process of completing the remediation efforts with respect to the material weakness described above.

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Our income tax accounting has significant complexity due to our business being property and equipment intensive, our varied types of refinancing and debt transactions, the significant number of foreign subsidiary legal entities and various tax planning strategies. To address this complexity, we restructured the United States tax department and hired both a senior manager of taxation for non-income tax matters and a Corporate Tax Director for oversight of the domestic, foreign and consolidated income tax responsibilities. In addition, we utilize third party tax advisors both to assist in the administrative and consolidation duties of preparing the income tax provision and disclosures and also to advise on matters beyond our in-house expertise. We believe that the personnel hired into these positions have the appropriate knowledge, experience and skills to maintain the proper controls over accounting for income taxes. However, the Corporate Tax Director has been in the position only since October 1, 2007, which, at December 31, 2007 was not enough time to remediate our internal controls over accounting for income taxes. We believe that during 2008, the Corporate Tax Director will have had enough time to remediate the controls related to documentation and historical analysis.

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**PART II. OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS**

The Company is subject to claims and legal proceedings that arise in the ordinary course of its business. Each of these matters is subject to various uncertainties, and it is possible that some of these matters may be resolved unfavorably to the Company. The Company believes that any aggregate liability that may result from the resolution of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

**ITEM 1A. RISK FACTORS**

A wide range of factors could materially affect our performance. In addition to factors affecting specific business operations and the financial results of those operations identified elsewhere in this report, the following factors, among others, could adversely affect our operations:

*Our disclosure controls and procedures and internal control over financial reporting were determined not to be effective as of December 31, 2007, which condition still existed at June 30, 2008, due to the material weakness that existed in our internal control over accounting for income taxes. Our disclosure controls and procedures and internal control over financial reporting may not be effective in future periods, as a result of existing or newly identified material weaknesses in internal control over financial reporting.*

In performing an internal control assessment at the end of 2006, our management identified a material weakness in our internal control over financial reporting, which condition still existed at June 30, 2008. A material weakness is a deficiency, or a combination of deficiencies, that adversely affects a company's ability to initiate, authorize, record, process, or report external financial data reliably in accordance with generally accepted accounting principles such that there is a more than remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected. For a discussion of the material weakness identified by our management, see Item 4. Controls and Procedures of our Quarterly Report on Form 10-Q for the period ended June 30, 2008. To address the material weakness, we performed additional analysis and other post-closing procedures in order to prepare our consolidated financial statements in accordance with generally accepted accounting principles. These additional procedures were costly, time consuming and required us to dedicate a significant amount of our resources, including the time and attention of our senior management, toward the correction of these problems. Performing these additional procedures in the future, could cause delays in the filing of our periodic and annual reports to the SEC.

The potential delay in the filing of our periodic and annual reports could have other adverse effects on our business, including, but not limited to: (1) civil litigation or an investigation by the SEC or other regulatory authorities, which could require us to incur significant legal expenses and other costs or to pay damages, fines or other penalties; (2) covenant defaults, and potentially events of default, under our senior secured credit facilities and the indentures governing our outstanding debt securities, resulting from our failure to file timely our financial statements; (3) negative publicity; and (4) the loss or impairment of investor confidence in our Company.

*If competitive pressures continue or intensify, we may not be able to service our debt or other obligations.*

There are substantial risks and uncertainties in our future operating results, particularly as aggressive pricing and bundling strategies by certain incumbent carriers, ILECs and other competitors, including cable companies, have intensified competitive pressures in the markets where we operate. In addition, regulatory decisions could have a material adverse impact on our competitive position, future operations and outlook. See also information under Item 2 MD&A Liquidity and Capital Resources Short- and Long-Term Liquidity Considerations and Risks and in these Risk Factors. If adverse events referenced or described herein or therein were to occur, we may not be able to service our debt or other obligations and could, among other things, be required to seek protection under the bankruptcy laws of the United States or other similar laws in other countries.

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***Our high level of debt and liquidity needs may adversely affect our financial and operating flexibility.***

We currently have substantial indebtedness and anticipate that we and our subsidiaries may incur additional indebtedness in the future. The level and/or terms of our indebtedness (1) could make it difficult for us to make required payments of principal and interest on our outstanding debt; (2) could limit our ability to obtain any necessary financing in the future for working capital, capital expenditures, debt service requirements or other purposes; (3) requires that a substantial portion of our cash flow, if any, be dedicated to the payment of principal and interest on outstanding indebtedness and other obligations and, accordingly, such cash flow will not be available for use in our business; (4) could limit our flexibility in planning for, or reacting to, changes in our business; (5) results in our being more highly leveraged than many of our competitors, which places us at a competitive disadvantage; (6) will make us more vulnerable in the event of a downturn in our business; and (7) could limit our ability to sell assets or fund our operations due to covenant restrictions. The recent tightening of the credit markets could also influence our ability to raise needed capital.

***Our common stock was delisted from the Nasdaq Capital Market, which could make it more difficult to sell our common stock.***

Effective at the open of trading on July 28, 2006, our common stock was delisted from the Nasdaq Capital Market. Since that time, our common stock has traded in the over-the-counter (OTC) market, both through listings on the OTC Bulletin Board and in the National Quotation Bureau

Pink Sheets, but our common stock is not currently listed or quoted on any recognized national or regional securities exchange or market. As a result, an investor may find it difficult to sell or obtain quotations as to the price of our common stock. Delisting could adversely affect investors perception, which could lead to further declines in the market price of our common stock. Delisting may also make it more difficult, time consuming and expensive for us to raise capital through sales of our common stock or securities convertible into our common stock.

***Given our limited experience in delivering individual and bundled local, wireless, broadband, DSL, Internet, data and hosting and VOIP services, we may not be able to operate successfully or expand these parts of our business.***

During the third quarter of 2004 we accelerated initiatives to become an integrated wireline, wireless and broadband service provider in order to counter competitive pricing pressures initiated by large incumbent providers in certain of the principal markets where we operate and to stem the loss of certain of our wireline and dial-up ISP customers to our competitors bundled wireless, wireline and broadband service offerings. Our experience in providing these products in certain markets and in providing these bundled service offerings is limited. Our primary competitors include incumbent telecommunications providers, cable companies and other ISPs that have a significant national or international presence. Many of these operators have substantially greater resources, capital and operational experience than we do. We are experiencing increased competition from traditional telecommunications carriers and cable companies and other new entrants that have expanded into the market for broadband, VOIP, Internet services, data and hosting and traditional voice services, and regulatory developments may impair our ability to compete. Therefore, future operations involving these individual or bundled services may not succeed in the competitive environment, and we may not be able to expand successfully; may experience margin pressure; may face quarterly revenue and operating results variability; may have limited resources to develop and to market the new services; and have heightened difficulty in establishing future revenues or results. As a result, there can be no assurance that we will reverse revenue declines in our legacy services or maintain or increase revenues or be able to generate sufficient income from operations or net income in the future or on any predictable or timely basis.

***We may be exposed to significant liability resulting from our noncompliance with FCC Orders regarding enhanced 911 (E911) services.***

In June 2005, the FCC adopted new rules requiring VOIP providers interconnected to the public switched telephone network to provide E911 service in a manner similar to traditional wireline carriers by November 2005. LINGO, a subsidiary of ours which sells such interconnected VOIP services, was unable, like many

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interconnected VOIP providers in the industry, to meet this deadline for all of its customers. We sought a waiver from the FCC asking for additional time to complete deploying our E911 service, and the FCC has not yet addressed our waiver petition. As of July 21, 2008, approximately 4.2% of our LINGO customers were without E911 service as required by the FCC's rules. If and to the extent that we are determined to be out of compliance with the FCC order regarding E911 services we may be subject to fines, penalties, and/or cease and desist orders prohibiting LINGO from providing service on the federal and state levels. However, at this time, management has determined the likelihood of incurring such fines or penalties to be remote.

The FCC rules also required interconnected VOIP providers to distribute stickers and labels informing customers of the emergency service limitations associated with the service, as well as to notify and obtain affirmative acknowledgement from customers that they were aware of all of the emergency service limitations associated with the service. The FCC's Enforcement Bureau released an order providing that the Enforcement Bureau will not pursue enforcement against interconnected VOIP providers that have received affirmative acknowledgement from at least 90% of their subscribers. We have received affirmative acknowledgement from substantially all of our customers and have effectively satisfied this requirement of the rule. LINGO's current services are more limited than the 911 services offered by traditional wireline telephone companies. These limitations may cause significant delays, or even failures, in callers' receipt of the emergency assistance. Despite the fact that we have notified our customers and received affirmative acknowledgement from substantially all of our customers that they understand the differences between the access we provide to emergency services as compared to those available through traditional wireline telephony providers, injured customers may attempt to hold us responsible for any loss, damage, personal injury or death suffered as a result of any failure to comply with the FCC mandated E911 service for interconnected VOIP providers. Our resulting liability could be significant.

On June 1, 2007, the FCC released a Notice of Proposed Rulemaking Proceeding considering the imposition of additional VOIP E911 obligations on interconnected VOIP providers, like us. Specifically, the Commission is considering requiring interconnected VOIP providers to determine automatically the physical location of their customer rather than allowing customers to manually register their location. Moreover, the Notice includes a tentative conclusion that all interconnected VOIP service providers that allow customers to use their service in more than one location (nomadic VOIP service providers such as us) must utilize automatic location technology that meets the same accuracy standards applicable to providers of mobile phone service providers. At this time, we are unable to predict the outcome of this proceeding or its impact on us.

On July 23, 2008, President Bush signed into law the New and Emerging Technologies 911 Improvement Act of 2008. Prior to enactment, interconnected VOIP providers, like us, did not have the same liability protection as wireline or wireless providers that offer emergency 911 calling services. The new law provides public safety entities, interconnected VOIP providers and others involved in handling 911 calls the same liability protections when handling 911 calls from interconnected VOIP users as from mobile or wired telephone service users. The applicability of the liability protection to 911 calling services that do not conform to the FCC's rules is unclear at this time. Additionally, any liability associated with 911 call placement and handling prior to the enactment of this new law would not be covered but we are currently unaware of any such liability.

***The FCC has extended CPNI rules to interconnected VOIP providers, which could limit our marketing efforts.***

On April 2, 2007, the FCC extended customer proprietary network information, or CPNI, rules to interconnected VOIP providers, like us. CPNI includes information that appears on customers' bills such as called telephone numbers, the frequency, duration, time and length of calls; and any services or features purchased by the consumer, like caller ID. Pursuant to the CPNI rules, interconnected VOIP providers may not use CPNI without obtaining customer consent except in limited circumstances. Moreover, interconnected VOIP providers are required to adhere to a particular customer approval processes when using CPNI outside of pre-defined limits. Effective December 8, 2007, we were required to adhere to specific CPNI rules when using

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CPNI for marketing purposes. Accordingly, we had to implement internal processes in order to comply with the FCC's CPNI rules. As required by the new rules, certifications were filed with the FCC regulating our compliance efforts in this regard. We cannot predict the impact of this change on our profitability or retail prices at this time.

### ***We may be exposed to liability resulting from FCC Orders regarding access for people with disabilities.***

On June 15, 2007, the FCC applied the disability access requirements of Sections 225 and 255 of the Communications Act to providers of interconnected VOIP services, like us, and to equipment manufacturers that make equipment to use with those services. Section 255 of the Communications Act requires, if readily achievable, service providers to ensure that its equipment and service is accessible to and usable by individuals with disabilities. Where readily achievable, the relevant regulations also require service providers to ensure that information and documentation provided in connection with equipment or services be accessible to people with disabilities and that employee training account for accessibility requirements. In addition, the FCC said that interconnected VOIP providers were subject to the requirements of Section 225, including contributing to the Telecommunications Relay Services, or TRS, fund and that they must offer 711 abbreviated dialing for access to relay services. At this time, we are not in compliance with these rules. We may be subject to enforcement actions including, but not limited to, fines, cease and desist orders, or other penalties. On October 10, 2007, the FCC granted a limited waiver of the 711 call handling requirement. While still mandating that interconnected VOIP providers like us are required to transmit 711 calls to a relay center, the FCC waived the requirement until March 31, 2009, insofar as it requires such providers to transmit the 711 call to an appropriate relay center, meaning the relay center(s) serving the state in which the caller is geographically located or the relay center(s) corresponding to the caller's last registered address. We are working on implementing a call routing solution which will route 711 calls to the appropriate relay center as defined in the FCC's order but cannot predict whether we will be in compliance at the end of the waiver period.

### ***Our profitability may be reduced or our retail prices may rise due to increased regulation or the imposition of additional taxes, fees and surcharges.***

On August 6, 2007, the FCC released a Report and Order regarding the collection of regulatory fees for Fiscal Year 2007 ( Fees Order ). Pursuant to the Fees Order, the FCC mandated the collection of such fees from interconnected VOIP service providers like us. The Fees Order mandates that interconnected VOIP providers pay regulatory fees based on reported interstate and international revenues. The Fees Order became effective in mid-November 2007. Regulatory fees for Fiscal Year 2007 will be due in 2008 during a separate filing window yet to be determined. Fiscal Year 2008 fees will also be paid in 2008 during the normal regulatory fee payment window. The assessment of regulatory fees to our service will increase our costs or cause us to increase the price of our retail service offerings and may have an adverse impact on our profitability.

We cannot predict the impact of any future laws, regulations and orders adopted either domestically or abroad on our operations and services. But increased regulation and the imposition of additional taxes, fees and surcharges increases the costs associated with providing our service and such taxes, fees and surcharges may or may not be recoverable from our customers. If we choose to absorb such costs, our profit margins would likely decrease. Moreover, even if such costs are recoverable or if we choose to maintain profitability, we may need to increase the retail price of our service that could result in making our service less competitive both with other providers of interconnected VOIP service providers and traditional providers of telecommunications services. The net effect could reduce the number of our subscribers, our revenue and our profit margin.

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*We are substantially smaller than our major competitors, whose marketing and pricing decisions, and relative size advantage, could adversely affect our ability to attract and to retain customers and are likely to continue to cause significant pricing pressures that could adversely affect our net revenues, results of operations and financial condition.*

The long distance telecommunications, Internet, broadband, DSL, data and hosting and wireless industry is significantly influenced by the marketing and pricing decisions of the larger long distance, Internet access, broadband, DSL, data and hosting and wireless business participants. Prices in the long distance industry have continued to decline in recent years, and as competition continues to increase within each of our service segments and each of our product lines, we believe that prices are likely to continue to decrease. Competitors in our core markets include, among others: AT&T, Verizon, the regional bell operating companies (RBOCs), cable companies and the major wireless carriers in the United States; Telstra, SingTel Optus and Telecom New Zealand in Australia; Telus, BCE, Allstream (formerly AT&T Canada) and the major wireless and cable companies in Canada; and BT, Cable & Wireless United Kingdom, Colt Telecom, Energis and the major wireless carriers in the United Kingdom. Customers frequently change long distance, wireless, broadband providers, and ISPs in response to the offering of lower rates or promotional incentives, increasingly as a result of bundling of various services by competitors. Moreover, competitors' VOIP and broadband product rollouts have added further customer choice and pricing pressure. As a result, generally, customers can switch carriers and service offerings at any time. Competition in all of our markets is likely to remain intense, or even increase in intensity and, as deregulatory influences are experienced in markets outside the United States, competition in non-United States markets is becoming similar to the intense competition in the United States. Many of our competitors are significantly larger than us and have substantially greater financial, technical and marketing resources, larger networks, a broader portfolio of service offerings, greater control over network and transmission lines, stronger name recognition and customer loyalty, long-standing relationships with our target customers, and lower debt leverage ratios. As a result, our ability to attract and retain customers may be adversely affected. Many of our competitors enjoy economies of scale that result in low cost structures for transmission and related costs that could cause significant pricing pressures within the industry. Several long distance carriers in the United States, Canada and Australia and the major wireless carriers and cable companies have introduced pricing and product bundling strategies that provide for fixed, low rates for calls. This strategy of our competitors could have a material adverse effect on our net revenue per minute, results of operations and financial condition if our pricing, set to remain competitive, is not offset by similar declines in our costs. Companies emerging out of bankruptcy might benefit from a lower cost structure and might apply pricing pressure within the industry to gain market share. We compete on the basis of price, particularly with respect to our sales to other carriers, and also on the basis of customer service and our ability to provide a variety of telecommunications products and services. If such price pressures and bundling strategies intensify, we may not be able to compete successfully in the future, may face quarterly revenue and operating results variability, and may have heightened difficulty in estimating future revenues or results.

*Our repositioning in the marketplace places a significant strain on our resources, and if not managed effectively, could result in operational inefficiencies and other difficulties.*

Our repositioning in the marketplace may place a significant strain on our management, operational and financial resources, and increase demand on our systems and controls. To manage this change effectively, we must continue to implement and improve our operational and financial systems and controls, invest in critical network infrastructure to maintain or improve our service quality levels, purchase and utilize other transmission facilities, and train and manage our employee base. If we inaccurately forecast the movement of traffic onto our network, we could have insufficient or excessive transmission facilities and disproportionate fixed expenses. As we proceed with our development, operational difficulties could arise from additional demand placed on customer provisioning and support, billing and management information systems, product delivery and fulfillment, on our support, sales and marketing and administrative resources and on our network infrastructure, maintenance and upgrading. For instance, we may encounter delays or cost-overruns or suffer other adverse consequences in implementing new systems when required, such as our off-shoring certain functions. In addition, our operating and financial control systems and infrastructure could be inadequate to ensure timely and accurate financial reporting, which could impact debt covenant compliance as well.

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***We have experienced significant historical, and may experience significant future, operating losses and net losses which may hinder our ability to meet our debt service or working capital requirements.***

As of June 30, 2008, we had an accumulated deficit of \$(1,031.3) million. We incurred net losses of \$(34.6) million in 2002, \$(10.6) million in 2004, \$(149.2) million in 2005, and \$(238.0) million in 2006. During the year ended December 31, 2003 and 2007, we recognized net income of \$54.8 million and \$15.7 million, respectively, of which \$39.4 million and \$32.7 million, respectively are the positive impact of foreign currency transaction gains. We cannot assure that we will recognize net income in future periods. If we cannot generate net income or sufficient operating profitability, we may not be able to meet our debt service or working capital requirements.

***Integration of acquisitions ultimately may not provide the benefits originally anticipated by management and may distract the attention of our personnel from the operation of our business.***

We strive to increase the volume of voice and data traffic that we carry over our existing global network in order to reduce transmission costs and other operating costs as a percentage of net revenue, improve margins, improve service quality and enhance our ability to introduce new products and services. We may pursue acquisitions in the future to further our strategic objectives. Acquisitions of businesses and customer lists, a key element of our historical growth strategy, involve operational risks, including the possibility that an acquisition does not ultimately provide the benefits originally anticipated by management. Moreover, there can be no assurance that we will be successful in identifying attractive acquisition candidates, completing and financing additional acquisitions on favorable terms, or integrating the acquired business or assets into our own. There may be difficulty in migrating the customer base and in integrating the service offerings, distribution channels and networks gained through acquisitions with our own. Successful integration of operations and technologies requires the dedication of management and other personnel, which may distract their attention from the day-to-day business, the development or acquisition of new technologies, and the pursuit of other business acquisition opportunities, and there can be no assurance that successful integration will occur in light of these factors.

***We experience intense domestic and international competition which may adversely affect our results of operations, financial condition, and cash flows.***

The local and long distance telecommunications, data, broadband, Internet, VOIP, data and hosting and wireless industries are intensely competitive with relatively limited barriers to entry in the more deregulated countries in which we operate and with numerous entities competing for the same customers. Recent and pending deregulation in various countries may encourage new entrants to compete, including ISPs, wireless companies, cable television companies, who would offer voice, broadband, Internet access and television, and electric power utilities who would offer voice and broadband Internet access. For example, the United States and many other countries have committed to open their telecommunications markets to competition pursuant to an agreement under the World Trade Organization which began on January 1, 1998. Further, in the United States, as certain conditions have been met under the Telecommunications Act of 1996, the RBOCs have been allowed to enter the long distance market, and other long distance carriers have been allowed to enter the local telephone services market (although judicial and regulatory developments have diminished the attractiveness of this opportunity), and many entities, including cable television companies and utilities, have been allowed to enter both the local service and long distance telecommunications markets.

***A deterioration in our relationships with facilities-based carriers could have a material adverse effect upon our business.***

We primarily connect our customers' telephone calls and data/Internet needs through transmission lines that we lease under a variety of arrangements with other facilities-based long distance carriers. Many of these carriers are, or may become, our competitors. Our ability to maintain and expand our business depends on our ability to maintain favorable relationships with the facilities-based carriers from which we lease transmission lines. If our



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relationship with one or more of these carriers were to deteriorate or terminate, it could have a material adverse effect upon our cost structure, service quality, network diversity, results of operations, financial condition, and cash flows.

***Uncertainties and risks associated with international markets and regulatory requirements could adversely impact our international operations.***

We have significant international operations and, for the three months ended June 30, 2008, derived 81% of our net revenues by providing services outside of the United States. In international markets, we are smaller than the principal or incumbent telecommunications carrier that operates in each of the foreign jurisdictions where we operate. In these markets, incumbent carriers are likely to control access to, and pricing of, the local networks; enjoy better brand recognition and brand and customer loyalty; generally offer a wider range of product and services; and have significant operational economies of scale, including a larger backbone network and more correspondent agreements. Moreover, the incumbent carrier may take many months to allow competitors, including us, to interconnect to our switches within our territory, and we are dependent upon their cooperation in migrating customers onto our network. There can be no assurance that we will be able to obtain the permits and operating licenses required for us to operate; obtain access to local transmission facilities on economically acceptable terms; or market services in international markets.

In addition, operating in international markets generally involves additional risks, including unexpected changes or uncertainties in regulatory requirements, taxes, tariffs, customs and duties. Given the nature of our operations and uncertainties in, or the absence of definitive regulations or interpretations concerning, the taxation of (including value added tax of) certain aspects of our business in certain international jurisdictions in which we conduct (or may be construed by such authorities as conducting or deriving taxable) operations or revenue, we may become subject to assessments for taxes (which may include penalties and interest) which are either unexpected and/or have not been accrued for in our historical results of operations. This circumstance occurred during March 2008, when we concluded it was probable that assessments would be forthcoming concerning past European prepaid calling services operations (see Management's Discussion and Analysis of Financial Condition and Results of Operations Results of Operations; Results of operations for the year ended December 31, 2007 as compared to the year ended December 31, 2006), and it is possible that tax uncertainties concerning our international operations could arise in the future. Such developments, in addition to the foregoing, could have adverse consequences that could result in restatement of prior period results of operations and unanticipated liquidity demands. Additional operating risks and uncertainties in operating in international markets include trade barriers, difficulties in staffing and managing foreign operations, problems in collecting accounts receivable, political risks, fluctuations in currency exchange rates, restrictions associated with the repatriation of funds, technology export and import restrictions, and seasonal reductions in business activity. Our ability to operate and grow our international operations successfully could be adversely impacted by these risks and uncertainties particularly in light of the fact that we derive such a large percentage of our revenues from outside of the United States.

***Because a significant portion of our business is conducted outside the United States, fluctuations in foreign currency exchange rates could adversely affect our results of operations.***

A significant portion of our net revenue is derived from sales and operations outside the United States. The reporting currency for our consolidated financial statements is the United States dollar. The local currency of each country is the functional currency for each of our respective entities operating in that country. In the future, we expect to continue to derive a significant portion of our net revenue and incur a significant portion of our operating costs outside the United States, and changes in exchange rates have had and may have a significant, and potentially adverse, effect on our results of operations. Our primary risk of loss regarding foreign currency exchange rate risk is caused by fluctuations in the following exchange rates: USD/AUD, USD/CAD, USD/GBP, and USD/EUR. See Quantitative and Qualitative Disclosures about Market Risk. Due to the large percentage of our operations conducted outside of the United States, strengthening or weakening of the USD relative to one

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or more of the foregoing currencies could have an adverse impact on future results of operations. We historically have not engaged in hedging transactions. During the fourth quarter 2007, we completed a forward currency contract required by a Canadian credit facility. In addition, the operations of affiliates and subsidiaries in foreign countries have been funded with investments and other advances denominated in foreign currencies. Historically, such investments and advances have been long-term in nature, and we accounted for any adjustments resulting from currency translation as a charge or credit to accumulated other comprehensive loss within the stockholders' deficit section of our consolidated balance sheets. In 2002, agreements with certain subsidiaries were put in place for repayment of a portion of the investments and advances made to those subsidiaries. As we anticipate repayment in the foreseeable future of these amounts, we recognize the unrealized gains and losses in foreign currency transaction gain (loss) on the consolidated statements of operations, and depending upon changes in future currency rates, such gains or losses could have a significant, and potentially adverse, effect on our results of operations.

***The telecommunications industry is rapidly changing, and if we are not able to adjust our strategy and resources effectively in the future to meet changing market conditions, we may not be able to compete effectively.***

The telecommunications industry is changing rapidly due to deregulation, privatization, consolidation, technological improvements, availability of alternative services such as wireless, broadband, DSL, Internet, VOIP, data and hosting and wireless DSL through use of the fixed wireless spectrum, and the globalization of the world's economies. In addition, alternative services to traditional fixed wireline services, such as wireless, broadband, Internet and VOIP services, are a substantial competitive threat. If we do not adjust to meet changing market conditions and if we do not have adequate resources, we may not be able to compete effectively. The telecommunications industry is marked by the introduction of new product and service offerings and technological improvements. Achieving successful financial results will depend on our ability to anticipate, assess and adapt to rapid technological changes, and offer, on a timely and cost-effective basis, services including the bundling of multiple services that meet evolving industry standards. If we do not anticipate, assess or adapt to such technological changes at a competitive price, maintain competitive services or obtain new technologies on a timely basis or on satisfactory terms, our financial results may be materially and adversely affected.

The rapid enhancement of VOIP technology may result in increasing levels of traditional domestic and international voice long distance traffic being transmitted over the Internet, as opposed to traditional telecommunication networks. Currently, there are significant capital investment savings and cost savings associated with carrying voice traffic employing VOIP technology, as compared to carrying calls over traditional networks. Thus, there exists the possibility that the price of traditional long distance voice services will decrease in order to be competitive with VOIP. Additionally, competition is expected to be intense to switch customers to VOIP product offerings, as is evidenced by numerous recent market announcements in the United States and internationally from industry leaders and competitive carriers concerning significant VOIP initiatives. Our ability effectively to retain our existing customer base and generate new customers, either through our traditional network or our own VOIP offerings, may be adversely affected by accelerated competition arising as a result of VOIP initiatives, as well as regulatory developments that may impede our ability to compete, such as restrictions on access to broadband networks owned and operated by others and the requirements to provide E911 services. As competition intensifies as a result of deregulatory, market or technological developments, our results of operations and financial condition could be adversely affected.

***If we are not able to operate a cost-effective network, we may not be able to grow our business successfully.***

Our long-term success depends on our ability to design, implement, operate, manage, maintain and upgrade a reliable and cost-effective network. In addition, we rely on third parties to enable us to expand and manage our global network and to provide local, broadband Internet, data and hosting and wireless services. If we fail to generate additional traffic on our network, if we experience technical or logistical impediments to our ability to

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develop necessary network or to migrate traffic and customers onto our network, or if we experience difficulties with our third-party providers, we may not achieve desired economies of scale or otherwise be successful in growing our business.

***If we are not able to use and protect intellectual property domestically and internationally, it could have a material adverse effect on our business.***

Our ability to compete depends, in part, on our ability to use intellectual property in the United States and internationally. We rely on a combination of trade secrets, trademarks and licenses to protect our intellectual property. We are also subject to the risks of claims and litigation alleging infringement of the intellectual property rights of others. The telecommunications industry is subject to frequent litigation regarding patent and other intellectual property rights. We rely upon certain technology, including hardware and software, licensed from third parties. There can be no assurance that the technology licensed by us will continue to provide competitive features and functionality or that licenses for technology currently used by us or other technology that we may seek to license in the future will be available to us on commercially reasonable terms or at all. Although our existing intellectual property are on standard commercial terms made generally available by the companies providing the licenses and, individually, their costs and terms are not material to our business, the loss of, or our inability to maintain existing licenses, could result in shipment delays or reductions until equivalent technology or suitable alternative products could be developed, identified, licensed and integrated and could cause service disruption to our customers. Such delays or reductions in the aggregate could harm our business. We also generally rely on indemnification provisions in licensing contracts to protect against claims of infringement regarding the licensed technology, which indemnification could be affected by, among other things, the financial strength of the licensor.

***The loss of key personnel could have a material adverse effect on our business.***

The loss of the services of K. Paul Singh, our Chairman and Chief Executive Officer, or the services of our other key personnel, or our inability to attract and retain additional key management, technical and sales personnel, could have a material adverse effect upon us.

***We are subject to potential adverse effects of regulation which may have a material adverse impact on our competitive position, growth and financial performance.***

Our operations are subject to constantly changing regulation. There can be no assurance that future regulatory changes will not have a material adverse effect on us, or that regulators or third parties will not raise material issues with regard to our compliance or noncompliance with applicable regulations, any of which could have a material adverse effect upon us. As a multinational telecommunications company, we are subject to varying degrees of regulation in each of the jurisdictions in which we provide our services. Local laws and regulations, and the interpretation of such laws and regulations, differ significantly among the jurisdictions in which we operate. Enforcement and interpretations of these laws and regulations can be unpredictable and are often subject to the informal views of government officials. Potential future regulatory, judicial, legislative, and government policy changes in jurisdictions where we operate could have a material adverse effect on us. Domestic or international regulators or third parties may raise material issues with regard to our compliance or noncompliance with applicable regulations, and therefore may have a material adverse impact on our competitive position, growth and financial performance. Regulatory considerations that affect or limit our business include (1) United States common carrier requirements not to discriminate unreasonably among customers and to charge just and reasonable rates; (2) general uncertainty regarding the future regulatory classification of and taxation of VOIP telephony, the need to provide emergency calling services in a manner required by the FCC that is not yet available commercially on a nation-wide basis and the ability to access broadband networks owned and operated by others; as regulators decide that VOIP is a regulated telecommunications service, our VOIP services may be subject to burdensome regulatory requirements and fees, we may be obligated to pay carriers additional interconnection fees and operating costs may increase; (3) general changes at the federal and/or state levels

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affecting access charges, universal service fund fees and regulatory fee payments would affect our cost of providing services; (4) ongoing regulatory proceedings regarding efforts by Telstra in Australia to increase prices and charges and to deny access to essential facilities; (5) the ultimate outcome of the process launched by the Australian government to help fund the construction of a new national broadband network, including whether and the terms upon which (a) we will have access to such network, and (b) the duration upon which the copper wire based last mile infrastructure needed by us to furnish broadband services using our DSLAM network infrastructure will be continued; (6) general changes in access charges and contribution payments could adversely affect our cost of providing long distance, wireless, broadband, VOIP, local and other services; and (7) regulatory proceedings in Canada determining whether and the extent to which regulation should mandate access to networks and interconnection including intra-exchange transport services which we use to interconnect our DSLAM collocation sites and high speed access to business services. Any adverse developments implicating the foregoing could materially adversely affect our business, financial condition, result of operations and prospects.

*Natural disasters may affect the markets in which we operate, our operations and our profitability.*

Many of the geographic areas where we conduct our business may be affected by natural disasters, including hurricanes and tropical storms. Hurricanes, tropical storms and other natural disasters could have a material adverse effect on the business by damaging the network facilities or curtailing voice or data traffic as a result of the effects of such events, such as destruction of homes and businesses.

*A small group of our stockholders could exercise influence over our affairs.*

As of February 29, 2008, funds affiliated with American International Group, Incorporated (AIG Entities) beneficially owned 13% of our outstanding common stock, which was acquired through the conversion of their Series C Preferred Stock. As a result of such share ownership, these holders can exercise influence over our affairs through the provisions of a certain Governance Agreement between such holders and us, dated November 4, 2003, that provide for their right to nominate a candidate for election by our stockholders to the board of directors and nominate one non-voting board observer, in each case subject to the maintenance of certain minimum ownership levels of our common stock and the board's right to exercise its fiduciary duties.

In addition, these holders' significant ownership levels could have an influence on: amendments to our certificate of incorporation; other fundamental corporate transactions such as mergers and asset sales; and the general direction of our business and affairs.

Also, the applicable triggering provisions of our rights agreement with StockTrans, Inc., as Rights Agent, dated December 23, 1998 (as amended, the Rights Agreement) contain exceptions with respect to the acquisition of beneficial ownership of our shares by such holders and the other former holders of Series C Preferred Stock. As a result, such holders could gain additional control over our affairs without triggering the provisions of the Rights Agreement.

Finally, certain stockholders, other than the AIG Entities, have from time to time made filings with the SEC to report beneficial ownership of our common stock at levels in excess of 5%. Such persons have reported beneficial ownership concerning approximately 42.1 million shares, in aggregate, as of December 31, 2007, and as a result, individually or in the aggregate, could potentially exercise influence over our business.

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

None.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES**

None.

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**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

At the Company's Annual Meeting of Stockholders held on June 19, 2008, the stockholders of the Company, holding 142,632,164 shares of record, elected K. Paul Singh, John F. DePodesta and Paul G. Pizzani to serve as Directors of the Company for a three-year term. The voting results were as follows: 102,831,220, 102,913,730 and 103,379,702 were in favor of Mr. Singh, Mr. DePodesta and Mr. Pizzani, respectively, and 4,344,129, 4,261,619 and 3,795,647 were withheld for Mr. Singh, Mr. DePodesta and Mr. Pizzani, respectively. John G. Puente, Douglas M. Karp, David E. Hershberg, and Pradman P. Kaul continued as directors of the Company after the meeting, along with Messrs. Singh, DePodesta and Pizzani.

**ITEM 5. OTHER INFORMATION**

None.

**ITEM 6. EXHIBITS**

(a) Exhibits (see index)

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**SIGNATURES**

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

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

Date: August 11, 2008

By: /s/ THOMAS R. KLOSTER  
Thomas R. Kloster  
*Chief Financial Officer (Principal Financial Officer)*

Date: August 11, 2008

By: /s/ TRACY B. LAWSON  
Tracy B. Lawson  
*Vice President Corporate Controller (Principal Accounting Officer)*

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**EXHIBIT INDEX**

| <b>Exhibit</b> |   |
|----------------|---|
| <b>Number</b>  | <b>Description</b>  |
| 3.1            | First amended and Restated Certificate of Incorporation of Primus; Incorporated by reference to Exhibit 3.1 of the Registration Statement on Form S-8, No. 333-56557.   |
| 3.2            | Certificate of Amendment to First Amended and Restated Certificate of Incorporation of Primus; Incorporated by reference to Exhibit 3.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2004. |
| 3.3            | Amended and Restated Bylaws of Primus; Incorporated by reference to Exhibit 3.2 to the Company's Annual Report on Form 10-K for the year ended December 31, 2002.   |
| 31             | Certifications.   |
| 32             | Certification.*   |

\* This certification is being furnished and will not be deemed filed for purposes of Section 18 of the Securities Exchange Act (15 U.S.C. 78r) and will not be deemed to be incorporated by reference into any filing under the Securities Act of 1933 or the Securities Exchange Act of 1934, except to the extent that the registrant specifically incorporates it by reference.