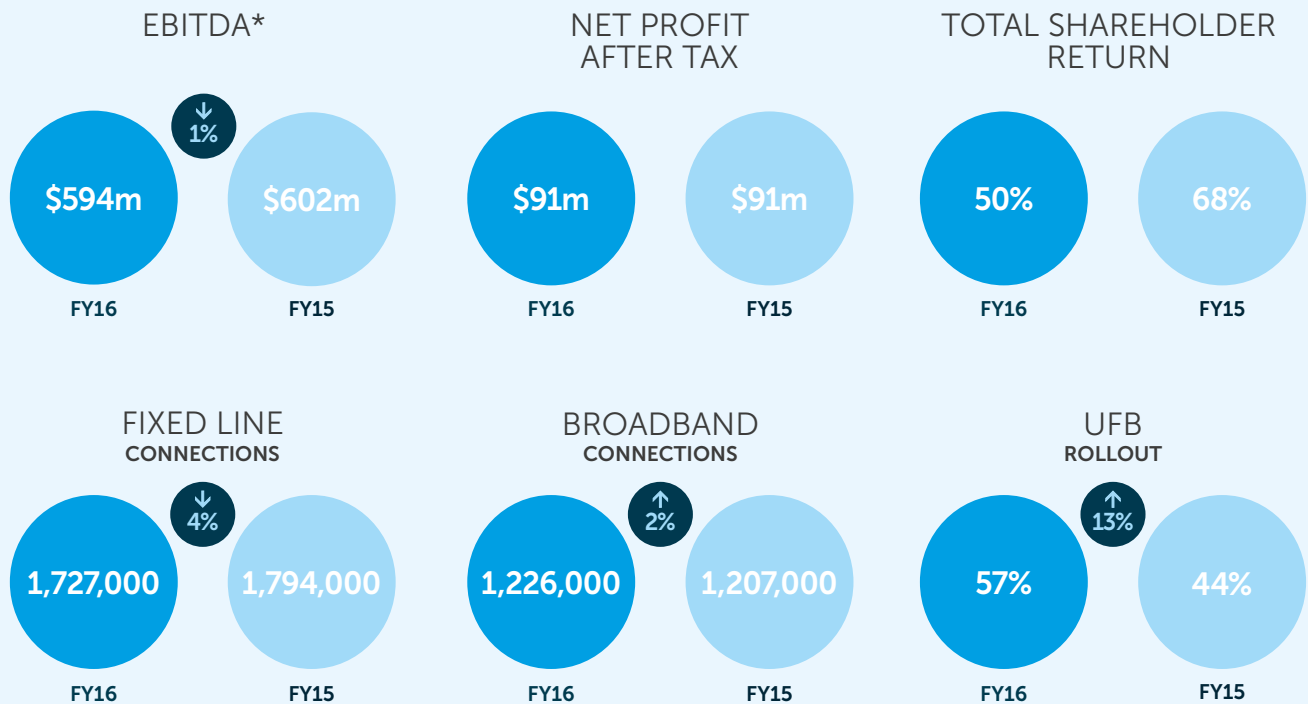




## Annual Report 2016

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## Highlights

Our Ultra-Fast Broadband (UFB) rollout has now passed 57% of planned premises and we've finished the Rural Broadband Initiative (RBI). Together with enhancements to our Very High Speed Digital Subscriber Line (VDSL) broadband service, these initiatives have made better broadband available to about 900,000 customers since we started in 2011.

Fibre connections on our network have exceeded 180,000 and continue to grow rapidly with about 12,000 connections completed in June 2016. Fibre uptake increased from 14% to 24% in our UFB areas and more than 50% of mass market connections are on a 100Mbps service or better.

We resumed dividend payments to shareholders after the Commerce Commission (the Commission) set copper pricing through to 2020 with the conclusion of its final pricing process. The Government has since announced high level policy decisions that include moving to a utility-style building block methodology for regulating fixed line copper and fibre services from 2020.

## Challenges

Despite doubling our workforce in the last 5 years, rapidly growing fibre demand means many customers are experiencing wait times to connect to fibre, while others have recently had to wait too long for faults on our copper network to be repaired. We're continuing to make process improvements across the industry, while also recruiting and training more people to provide a better experience for customers.

Total fixed line connections are declining as other fibre networks benefit from customer demand and mobile network operators promote wireless broadband options.

Lack of regulatory certainty post 2020 makes it commercially challenging for us to make significant new investments, including additional UFB and RBI investment.

\* Earnings before interest, income tax, depreciation and amortisation (EBITDA) is a non-GAAP profit measure. We monitor this as a key performance indicator and we believe it assists investors in assessing the performance of the core operations of the business.

## Chorus Board and management overview




**Patrick Strange**  
Chairman




**Mark Ratcliffe**  
Managing Director and CEO

This report is dated 29 August 2016 and is signed on behalf of the Board of Chorus Limited.

### Dear Shareholders

This time last year we were managing the business to preserve cash and dividends had been suspended since late 2013. Fast-forward to today and it is a much improved operating context. The Commerce Commission's final copper pricing decision in December 2015 provided a better pricing path to 2020 than indicated by their earlier benchmarking and draft decisions. This enabled us to begin investing again to strengthen our network and service capability for customers. However, much more remains to be done to improve the customer experience, particularly as we need to balance the growing demand for fibre connections with our workforce requirements to maintain the existing network.

Substantial network investment through our ongoing UFB rollout, the now completed RBI rollout and enhancements to our VDSL service have made better broadband available to about 900,000 customers since we were established in 2011. These network upgrades are coinciding with a dramatic surge in broadband traffic. Broadband as the emerging fourth utility clearly sits at the heart of the home and is playing a pivotal role in New Zealanders' day-to-day lives.

Our financial metrics for the period were still affected by the five and a half months under which benchmarked copper prices applied to our key copper services.

However, EBITDA of \$594 million was at the top end of the guidance we provided for FY16, reflecting continued good cost management across the business. Importantly, we were able to start managing the business for long-term shareholder value.

In February we announced the resumption of dividends and our expectation of providing shareholders with modest long term dividend growth during the UFB build programme to 2020. The greater regulatory clarity meant we could diversify our bank debt funding, in place since 2011, through a \$400 million bond issue and refinance our existing bank debt to deliver material cost savings.

Together, the restoration of some clarity to our regulatory environment and the operating momentum within the business helped our share price appreciate 46% during the period. Our market capitalisation has increased from about \$1.1 billion to \$1.8 billion and we've recently been readmitted to the S&P/NZX 20 Index. It's a positive turnaround, but the copper pricing outcome has not restored our financial position to demerger levels and the regulatory framework that may apply from 2020 remains far from clear. We are therefore continuing to take a measured approach to ongoing investment.

# Bringing New Zealand better broadband

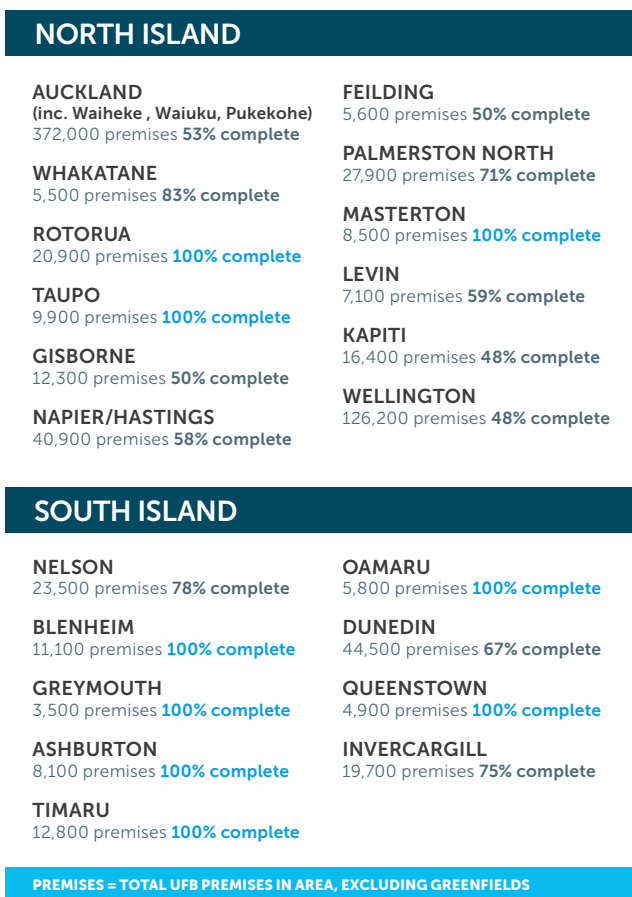
There's no question that broadband has become an essential utility – much like electricity, water and gas. We recognise we need to provide the best network and service possible if we're to continue to grow broadband connections on our network.

About 640,000 customers are now within reach of our UFB network and we're now 57% of the way through the rollout. Uptake rose to 24%, up from 14% at the start of the financial year. We built fibre to the boundary of 106,000 more premises during the period.

This included finishing the rollout in Greymouth, Masterton, Queenstown, Rotorua and Waiuku.

Rural areas also benefitted during the year with the final phase of the RBI extending fibre to our upgraded broadband cabinets and new Vodafone tower sites. The five-year rollout was completed at the lower end of our initial capital expenditure guidance range of \$280-\$295 million and we delivered more coverage than originally contracted by Government.

Figure 1: Progress by Chorus UFB Area as at 30 June 2016

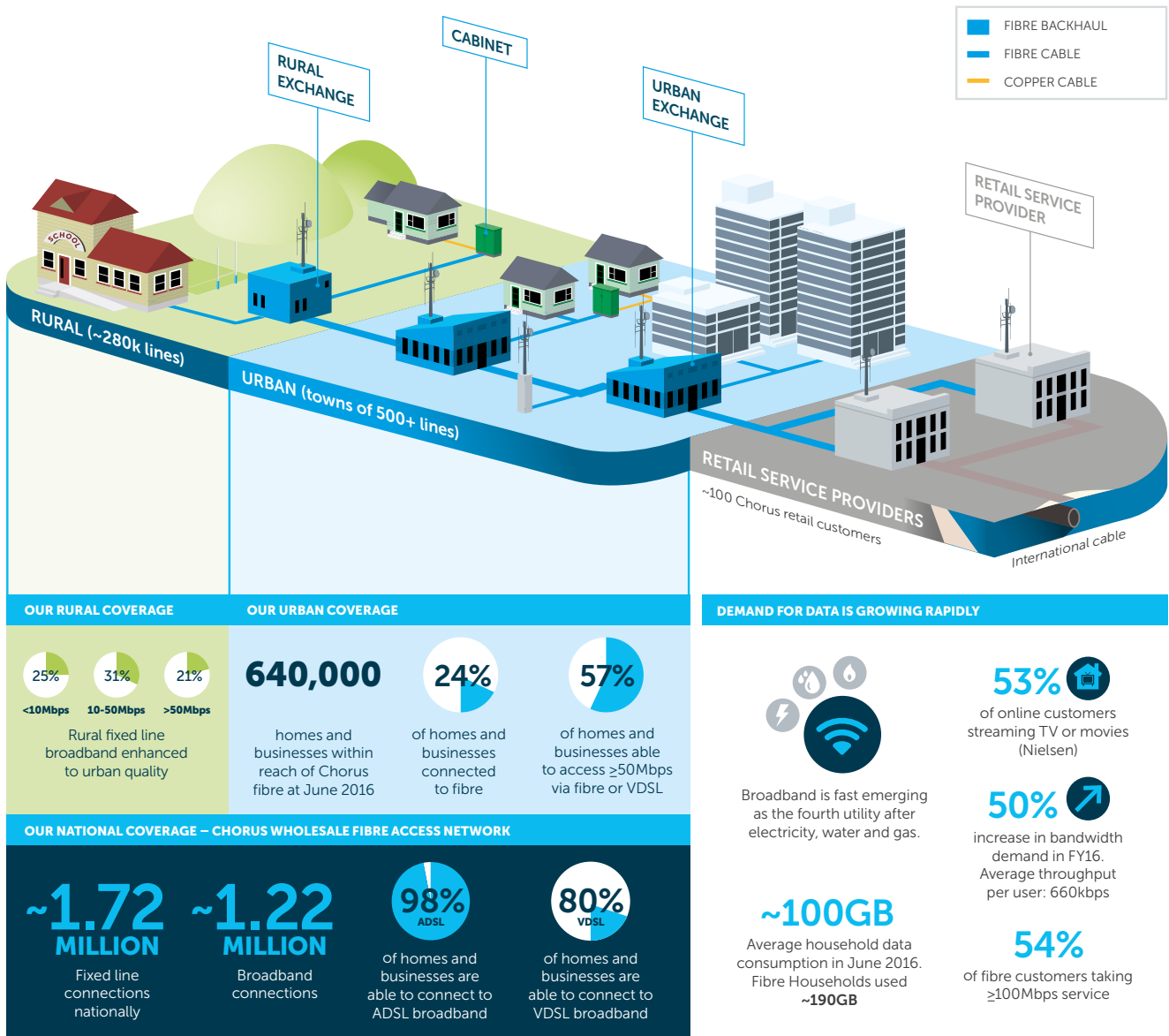


We deployed about 3,500 kilometres of fibre to rural schools and hospitals and enhanced our broadband coverage to approximately 110,000 rural homes and businesses.

About 50% of rural customers should now be able to access broadband speeds on our network of 10Mbps or better, with about 20% able to access speeds in excess of 50Mbps (see Figure 2). The benefits of retail competition across our wholesale network footprint are also evident with uptake within our RBI areas reaching about 88%.

During the year, a change in the frequencies used to transmit VDSL broadband saw average peak speeds on VDSL rise from 35Mbps to 50Mbps. It also enabled us to increase our VDSL footprint by an estimated 175,000 customers. The combination of UFB, RBI and VDSL upgrades means we now have high-speed broadband available via fibre or copper-based VDSL technology across 85% of our broadband capable lines. By 2020, our fibre footprint will have increased from about a third of broadband capable connections to 60%.

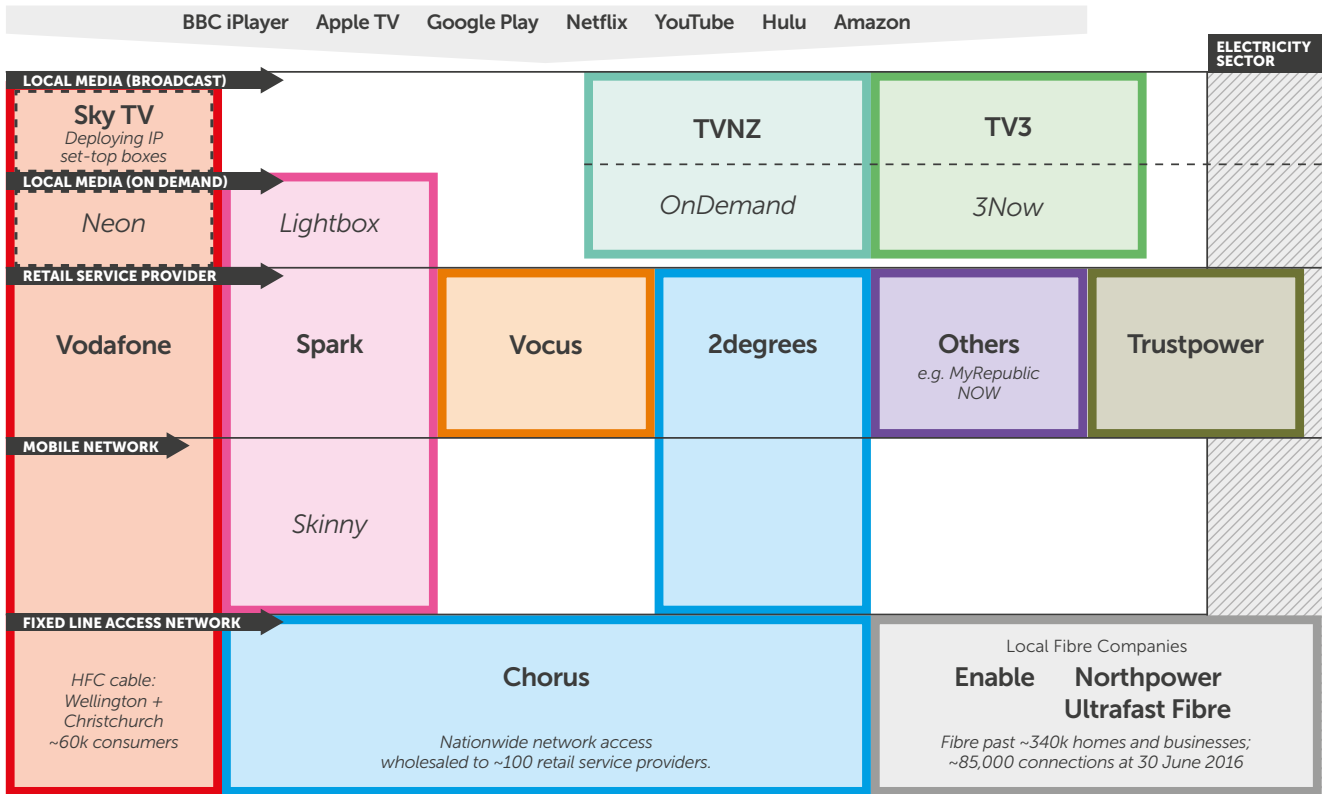
Figure 2: The Chorus Network: bringing better broadband



# Market overview

**Figure 3: The New Zealand fixed line market**

Rationalisation, new entrants and new business models are disrupting the NZ market



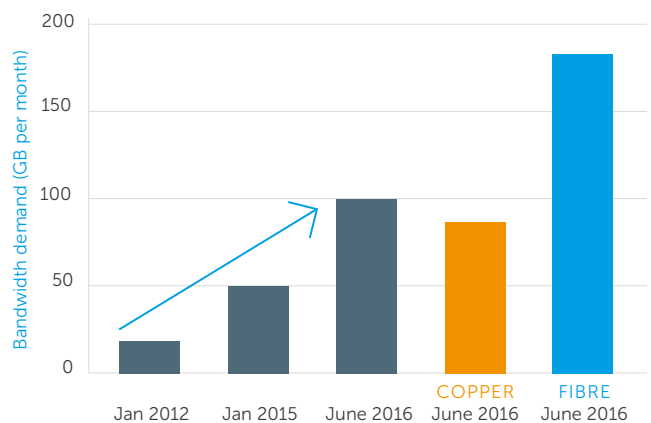
The New Zealand retail market has been through a period of significant consolidation, particularly amongst second tier providers. In February 2016 Vocus finalised its merger with M2 which had bought the Callplus group in April 2015. In July 2016 Sky TV shareholders approved a proposal to merge with Vodafone New Zealand and this is now subject to final Commission approval.

For the most part, retailers are now focused on growing their relative shares of the broadband market and this has spurred significant price-based competition with some providers offering high-speed plans at much reduced prices for the initial year of a two-year contract.

Another market dynamic in the last year is the shift in retail focus from the 30Mbps entry level fibre service to the 100Mbps service. Most retailers now promote the 100Mbps service as their default fibre product and have encouraged existing fibre customers to upgrade their service with special offers. As a result, by the end of the period we had 54% of mass market fibre customers on plans of 100Mbps or higher, up from 32% at the end of FY15.

The proliferation of easy to access online video content, particularly Netflix and YouTube, has continued to drive an upsurge in the amount of bandwidth consumed over our network. In January 2012 the average household monthly bandwidth demand across our network was 13 gigabytes (GB). By January 2015 it had increased to 50GB and by June 2016 it had doubled to 100GB (see Figure 4).

**Figure 4: Average household bandwidth demand on our network**



Three factors are driving this data tsunami. First, the broadband pipe is no longer connected just to a computer desktop. The average New Zealand home now has about four smart devices routinely connecting to the internet. When we install a fibre connection it is typically behind a smart TV and everyone in the home may be online at any time.

Second, the floodgates have been opened by retail service providers. In 2012 the typical datacap was 20GB a month. Now it's estimated that about half of households have chosen unlimited data plans. Most providers now offer 80GB as a minimum datacap.

The third and most significant factor, is the content itself. A Nielsen survey earlier this year suggested 53% of online customers in New Zealand are streaming TV or movies. Roy Morgan research suggests more than 900,000 Kiwis now use a Netflix, Lightbox (Spark) or Neon (Sky TV) subscription streaming service. It's estimated that video content now typically accounts for up to three quarters of a retail provider's broadband traffic.

Bandwidth consumption is expected to grow as video streaming becomes more mainstream and uptake of high-speed broadband increases. Streaming an hour of high definition (HD) video uses between 2GB to 3GB of data. We're already seeing households with fibre connections use an average of about 190GB a month. That's double the average for households on our copper network. The adoption of Ultra HD 4K TV and future 8K TV devices will only increase this. Vodafone is already multicasting Sky TV programming over our fibre network and Sky TV is currently upgrading all its digital decoders to enable on-demand viewing of its content.

The surge in bandwidth demand is good news for fixed line networks such as ours. We're able to provision capacity across much of our network to ensure sustained capacity is available to each customer during peak night time viewing hours. This is a key competitive advantage for fixed line networks relative to current wireless network technologies which must share capacity amongst each additional customer. If customers don't have a good peak speed service and sustained network capacity to match, they may be frustrated by things like screen freezes during their favourite programmes.

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## Connecting customers

Our number one operational priority has been improving the fibre connection experience for customers. We made good progress, with a substantial number of changes made to the way we work with our retail service provider customers and interact with customers. However, we know we're still not providing a good experience for too many customers and our focus on this continues.

Our initiatives included setting up a team to contact customers and reconfirm scheduled visits. This helped ensure correct details are in our systems and reduced wasted technician visits. We also proposed taking on more responsibility and managing all customer interaction for our retail service provider customers, from when they receive a customer's fibre order through to activation of the service. Our proposal included covering the cost of this additional support through to the end of December 2016. Not all providers have opted to use our support function, with some focused on automating their own provisioning processes instead. For providers using our support function, we launched an online order tracker in April so customers can easily access up to date information about our progress with their fibre connection.

At the same time as we've been refining our connection processes, demand for fibre has increased dramatically. During FY16 monthly fibre order volumes grew by 60%. Our biggest challenge is hiring people quickly enough to deal with this volume of demand. It takes between three to six months to train up a new fibre technician, as it requires a wide range of skills, including customer service, hard physical work and sometimes quite technical installations inside the property.

During the financial year we worked closely with our service company partners to almost double the number of fibre field crews from 275 to 524. As a result of this and process improvements, we lifted the number of connections completed in a month from about 6,000 in July 2015 to 12,000 in June 2016. In all, we processed more than 110,000 connections during the year. This is a significant achievement when you consider that it appears to be about twice the connection volume of Sky TV's busiest ever year. They had a much less extensive or intrusive installation process and are the closest parallel for a large scale deployment.

However, the rapid increase in our workforce saw the quality of some installations fall below our expected standards and we're continuing to address this. In July 2016 we apologised to customers who'd been waiting too long for faults on our copper network to be repaired, following wet winter weather and major cable cuts by third parties. This reflected the challenge of balancing growing workforce demands between our new fibre network and the existing copper network. We're currently looking to recruit another 250 technicians and support staff by the end of 2016.

## Network competition

As expected since the start of the UFB and RBI rollouts, we're beginning to see some line loss to other fibre and wireless networks. This is reflected in the reduction in our total fixed line count from 1,794,000 in FY15 to 1,727,000 at the end of this period.

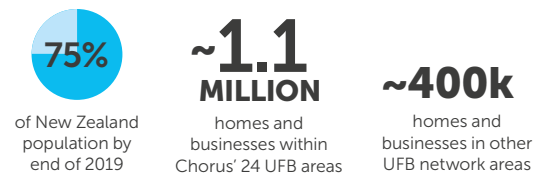
The Government's other UFB partners – Northpower, Ultra-fast Fibre and Enable – had passed an estimated 340,000 homes and businesses by the end of the period. They too are experiencing strong fibre uptake and have connected an estimated 85,000 customers, up from approximately 35,000 at the end of FY15.

We also compete with Vodafone's cable network in the Wellington area where we are building the UFB network and in Christchurch where we have our existing network. Vodafone has announced it intends to upgrade its cable network and offer 1Gbps services in 2016.

We've begun to see some line loss to wireless networks, particularly in rural areas where our network currently has limited backhaul capacity. This has been expected given Vodafone's rural broadband contract with the Government to provide wireless broadband coverage to 80% of rural households. Wireless competition is expected to grow now that Spark has launched fixed wireless broadband services in rural and urban areas. The technical constraints of fixed wireless networks means these services have datacap limits, while unlimited data plans are now typically promoted by retailers for fixed line services.

**Figure 5: Building a fibre to the premises network**

Ultra-Fast Broadband partnerships with the Crown cover 33 areas.



**CHORUS UFB BUILD METRICS**

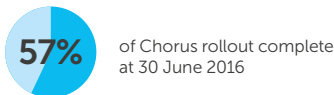
**\$1.75 – \$1.8 billion** Estimated cost of Chorus communal network to pass

**\$929 million** funding contribution from the Crown equates to

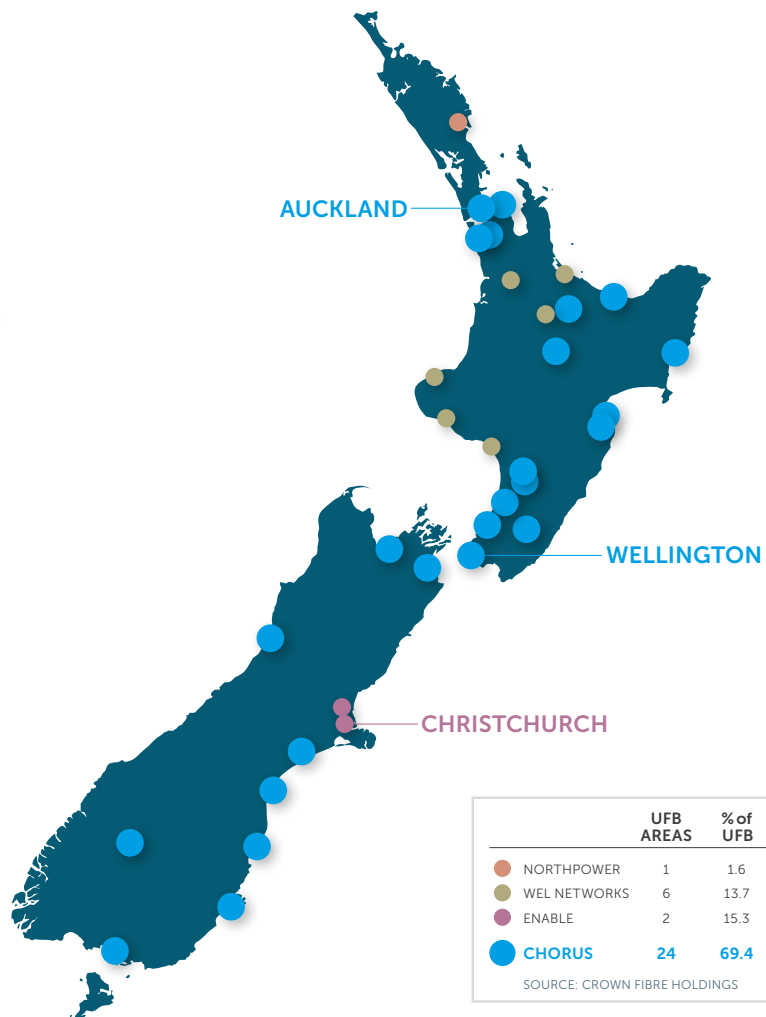
**830,900** premises

**\$1,118** per premises passed

Chorus issues debt and equity securities to the Crown in return. Debt to be redeemed in tranches from 2025 to 2036. Increasing portion of the Crown equity attracts dividend payments from 2025 onwards.



Connections from the street boundary to the premises are completed on demand. Estimated cost of **\$900 – \$1,100** (in 2011 dollars) average cost to connect standard residential premises.





## Health and safety

Keeping people healthy and safe is a priority. No business objective will be prioritised over the health and safety of any person in our work environments. We're focused on maturing to a resilient culture in our health and safety systems and practices. We're heading in the right direction but have a lot more work to do. We have a strong and visible commitment to an open reporting culture and one of continuous improvement.

Our nationwide presence and the significant investment happening in broadband infrastructure means we're uniquely placed to provide leadership in the health and safety of our employees and with our contracted partners. Key risks in the field include working at heights and in confined spaces, driving, asbestos, and striking other networks and electrocution.

We're committed to taking all reasonably practicable steps to ensure a safe and secure environment for our people (including employees and contractors) and anyone who is in, or in the vicinity of, our workplaces. We're concerned that there was a significant injury from a ladder fall in the reporting period and another one shortly after. Either could've been fatalities.

We have a significant programme of work which continues to improve our health and safety practices and we continue to work closely with our contractors on reducing the risk of work related injuries. We regularly carry out audits of field work and will shut down sites where our health and safety standards aren't being met. During the 10.7 million hours worked in FY16 we, including our five service companies, recorded the following rates (based on one million hours worked):

- Total Recorded Injury Frequency Rate of 5.77 (this is lost time injuries + medical treatment injuries + restricted work injuries divided by total work hours x 1,000,000. This is a global standard that we can use to benchmark ourselves).
- Lost Time Injury Frequency Rate of 1.86 (this is the number of lost time injuries divided by total work hours x 1,000,000. Again, this is a global measure).

### Our health and safety focus over the last year includes:

- Active engagement with our contractors, our industry and other infrastructure industries at strategic and operational levels.
- Screening 1,500 of our contractors and suppliers to ensure their systems and procedures meet our health and safety expectations.
- Developing and putting all service company technicians (around 2,500) through a work training competency programme for field work. The programme is now endorsed by the New Zealand Qualifications Authority and all technicians must complete the programme before they can work on our network.
- Replacement of our vehicle fleet with 5-Star New Car Assessment Programme rated vehicles and GPS tracking.
- Increased driver awareness activities with refreshment of driving policies and increased training.
- Continuously improving our health and safety management system, policies and practices.
- Reviewing and improving reporting practices.
- Reviewing our risk and control awareness and assessments.
- Ongoing asbestos and earthquake prone building assessments.
- Staff engagement surveys showing a positive reflection on embracing health and safety as part of "how we do things around here".
- Implementing a company-wide wellbeing programme centred around four components of physical, emotional, career and wider world.
- Working towards a higher level of ACC accreditation.
- The Board commissioning an independent external review to objectively assess our current state and support our maturity, programme of work and future resourcing requirements.

## Governance and corporate sustainability

The Chorus Board is committed to good governance practices and more detail on these is available in the Governance and Disclosures section, as well as a separate Corporate Governance statement available on our website. The Board has overall responsibility for strategy, culture, health and safety and governance. Dr Patrick Strange was appointed chairman from 1 September 2015 and Jon Hartley, who had been interim chairman since April 2015, became deputy chairman. Murray Jordan also joined the Board from 1 September 2015.

We continue to demonstrate excellence in employee engagement, leadership effectiveness and a high-performance culture. For the fifth consecutive year we received best employer accreditation with

an employee engagement score of 83%, a slight increase on 82% in 2015 when we also became the first New Zealand company to win the Best of the Best supreme award in the Aon Hewitt Best Employer Awards.

We're active in local communities through our cabinet art and volunteer day initiatives. We funded more than 90 local artists to paint murals on almost 100 of our broadband cabinets during the year, helping reduce the impact of graffiti on our network and raise community engagement through art. In selecting artists we look for designs that fit the local environment and reflect the local community.

## Governance and corporate sustainability (cont.)

About 350 of our people helped their local communities through the use of their sponsored volunteer day with activities such as tree planting, helping out in local hospices and other community projects. Employees also used our payroll giving programme to donate to local charities.

We've continued to work closely with GigCity Dunedin to make the most of our sponsored gigabit broadband services being rolled out across the city after they won our Gigatown competition in late 2014. As well as bringing forward the timeframe to complete the fibre rollout in Dunedin by two years, we helped launch a public access Wi-Fi service in the central business area and have so far contributed about \$140,000 to a community fund for innovators exploring the use of fibre to enhance the development, experimentation and implementation of community, learning and workforce opportunities in Dunedin.

At a national level, our support for innovation includes the New Zealand Innovation Partnership; the Health and Science category sponsor of the New Zealand Innovators Awards and

CO.STARTERS, a programme that helps create a strong support network for business start-ups.

Our investment in better broadband networks is helping establish a platform for low-carbon communities by extending the availability of new and emerging communications functionality and applications. Our own commitment to a sustainable operating model includes annual carbon reporting to CDP, an organisation that has gathered the largest global collection of self-reported companies' environmental information. Network electricity consumption and our field service vehicle fleet account for more than 90% of our greenhouse gas emissions.

Our data shows we've reduced our annual emissions by 25% since our FY12 base year, with a 5% reduction in FY16. We've achieved this by reducing our own direct emissions, limiting growth in our consumption of electricity and working with our third party service providers to manage vehicle fleet emissions. We also have a waste management strategy and are continuing to remove ozone depleting substances from our network.

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## Regulatory developments

### Government review of telecommunications regulatory framework

The Government is currently consulting on how communications services should be regulated after 2020 with the goal of establishing "...a durable and flexible framework that supports competition, innovation, and efficient investment for consumers."

On 14 April 2016 the Government announced a series of high-level policy decisions on its review, including:

- Moving to a utility-style building block methodology for regulating both fixed line copper and fibre wholesale services;
- The utility-style model could include anchor products for basic voice and basic broadband with reference to entry level prices in the market; and
- Retaining the current unbundling requirements on the UFB network from 2020.

Further consultation on detailed design and implementation issues was announced on 12 July 2016 with the Government's release of an options paper seeking submissions by 2 September. The paper indicates that a more fit for purpose regime can be put in place by 2020, with legislation to be passed in 2017.

### Final Pricing Principle (FPP) determination

Copper and fibre price relativity was restored when the Commission released its final pricing determinations on 15 December 2015.

The Commission announced aggregate copper pricing that starts at \$41.19 a month and reaches \$42.35 in 2020. These prices improved on the initial benchmark pricing, but are still below the \$45.92 aggregate price that applied in 2011 when Chorus was established. This appears to be a function of the Commission's use of trenching costs well below our actual costs and the exclusion of portions of our existing network footprint. The weighted average cost of capital also declined substantively due to methodology changes and process delays coinciding with reductions in market risk free rates.

When combined with a reduction of about 25% on transaction charges we incur for service company activity, the effect is a reduction of around \$50 million per annum in our EBITDA from 2011 levels. We elected not to appeal the decision, despite disagreeing with some key elements, because we believed the best long-term value for shareholders would be achieved by removing any ongoing legal uncertainty.

For a more detailed overview of our regulatory environment, please see the *Regulation, legislation and litigation* section in the management commentary.

## Outlook

We're placing renewed focus on Chorus' place within New Zealand's broadband ecosystem and our goal of bringing New Zealand better broadband. We recognise that to achieve this we need to become a more customer-oriented broadband company. We know we have a quality product and we need the customer service experience to match that for all customers, not just most.

We've already made a start with our efforts to improve the fibre connection process for customers, but much remains to be done. Consistently meeting demand and delivering a high-quality connection experience remains our number one operational priority. We'll continue streamlining processes and driving the recruitment of more technicians.

You'll also see us continue taking a more active role in promoting the broadband options already available to New Zealanders. We've begun by revamping our website to be more customer focused. You can now enter your address to learn your current broadband speed on our network and whether better options are available. We know that about 60% of households could already get faster broadband than they currently have by subscribing to, for example, VDSL or a 100Mbps fibre plan. Some retailers are already offering the best available technology – be it ADSL, VDSL or fibre – at the same retail price.

In line with our customer focus, we're investing more to ensure that our broadband network enables increasing bandwidth consumption and performs as expected. We believe fixed line networks can provide the best broadband experience for customers, particularly with sustained speeds needed at peak demand times for optimal video streaming. A recent Cisco report predicts internet traffic in New Zealand is likely to double by 2020 when it will reach the equivalent of more than 72,000 DVDs per hour. Our own forecast is that monthly household data usage will grow from the current average of 100GB to 170GB by June 2017.

The merger of Sky TV and Vodafone could increase bandwidth demand further again. Part of the reported rationale for the merger is an intention to drive the increased penetration of subscription television by making content available as widely as possible and across more delivery platforms. This includes the opportunity to

reduce satellite capacity over the medium to long-term with a shift to fibre.

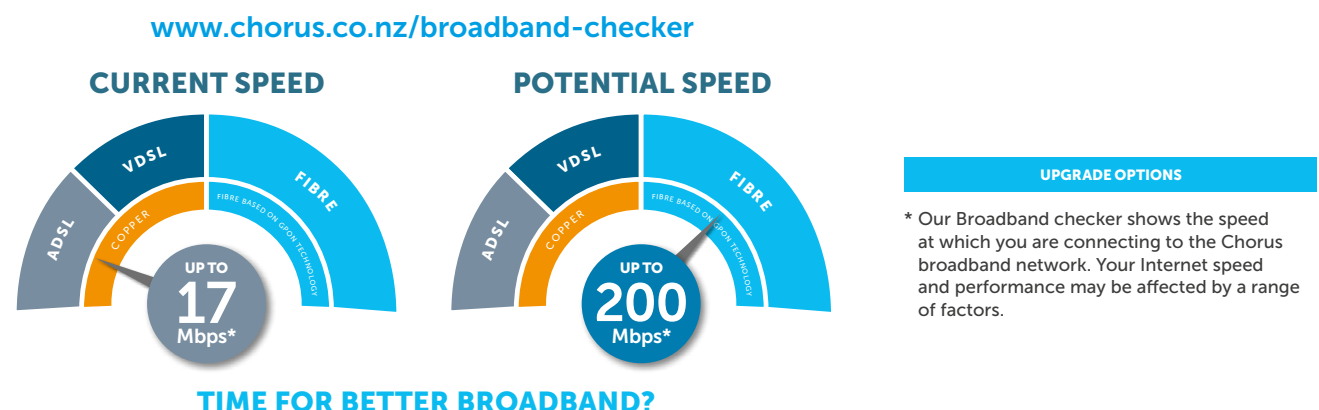
We do face growing network competition from local fibre companies and expect our overall connections to continue to reduce as their UFB networks gain more market share. However, we continue to operate and promote our high-speed VDSL and business fibre networks in these areas. The pace of line loss will be partially offset by ongoing population and housing growth elsewhere, particularly in the Auckland region. Vertically integrated mobile network providers are also promoting wireless broadband as a fixed line broadband alternative. The extent of this competition remains to be seen given the limited datacaps provided, the rise of video streaming and the strong retail competition promoting the increasing capability of our fibre and copper broadband network.

The Government is seeking to extend the UFB network beyond the current planned footprint to at least another 5% of New Zealanders by the end of 2022 and extend investment in rural broadband by another \$100 million. Updates on both initiatives are expected this financial year. The challenge is that the details of the proposed new regulatory framework are still to be decided. This makes it difficult to assess what returns are likely on any new investment. As we've said previously, we're interested and willing to participate in these initiatives if a fair return can be earned on our investment and there is long-term value for shareholders.

We've invested about \$2.9 billion in capital expenditure since our business was established in 2011, with \$593 million of that during FY16 alone. A regulatory framework that recognises broadband as an essential utility is necessary if New Zealand is to encourage ongoing improvement and extension of its broadband capability. As we saw during the copper pricing process, uncertainty dampens investment and leads to poorer customer outcomes.

We welcome the Government's current review of the regulatory framework for communications services and believe it is an opportunity to align and deliver on the interests of customers and investors. A stable transition in pricing at 2020 is central to this and could help New Zealand achieve better broadband coverage well beyond the Government's current goals.

Figure 6: Check the Chorus broadband options at your address





**Patrick Strange**  
BE (Hons), PhD

Chairman  
Independent Director since 6 April 2015  
Chairman of Nominations and Corporate Governance Committee  
Member of Audit and Risk Management Committee

Dr Patrick Strange has spent 30 years working as a senior executive and director in both private and listed companies, including for more than six years as Chief Executive of Transpower where he oversaw Transpower's \$3.8 billion of essential investment in the National Grid. Patrick is currently a director of Mercury NZ, Auckland International Airport, NZX Limited and the boards of Ausgrid, Endeavour Energy and Essential Energy, Australia.



**Jon Hartley**  
BA Econ Accounting (Hons), Fellow ICA (England & Wales),  
Associate ICA (Australia), Fellow AICD

Deputy Chairman  
Independent Director since 1 December 2011  
Member of Nominations and Corporate Governance Committee  
Member of Audit and Risk Management Committee

Jon is a Chartered Accountant and Fellow of the Australian Institute of Company Directors. He has held senior roles across a diverse range of commercial and not for profit organisations in several countries, including as chairman of SkyCity, director of Mighty River Power, CEO of Brierley New Zealand and Solid Energy, and CFO of Lend Lease in Australia. Jon is currently deputy chairman of ASB Bank and Sovereign Assurance Company, chairman of VisionFund International and the Wellington City Mission and a trustee of World Vision New Zealand.



**Anne Urlwin**  
BCom, CA, F InstD, FNZIM, ACIS

Independent Director since 1 December 2011  
Chairman of Audit and Risk Management Committee

Anne is chairman of Naylor Love Enterprises and a director of Southern Response Earthquake Services, Steel & Tube Holdings, OnePath Life (NZ) and Summerset Group. Anne is also the independent chairman of the Ngai Tahu Te Runanga Audit and Risk Committee. Her previous directorship experience encompasses many sectors, including energy, health, construction, regulatory services, internet infrastructure, research, banking, forestry and the primary sector, as well as education, sports administration and the arts. She is the former chairman of Lakes Environmental, the New Zealand Blood Service, the New Zealand Domain Name Registry and a former director of Meridian Energy.



**Clayton Wakefield**  
BSc (Computer Science), GradDip Mgmt, CMIInstD

Independent Director since 1 December 2011  
Member of Human Resources and Compensation Committee

Clayton has over 30 years' experience in the banking, financial services, telecommunications and technology industries and is a Chartered Member of the Institute of Directors. Clayton is a director of The Co-operative Bank, a former director of Endace and Fisher & Paykel Finance and its subsidiaries, a former chairman of Electronic Transactions Services and Visa New Zealand, and a former executive director and owner of Techspace. From 2001 to 2007 Clayton was Head of Technology and Operations at ASB Bank.



**Keith Turner**

BE (Hons), ME, PhD DistFIPENZ

Independent Director since 1 December 2011  
 Member of Human Resources and Compensation Committee  
 Member of UFB Steering Committee

Dr Keith Turner was CEO of New Zealand electricity generator and retailer Meridian Energy for nine years from its establishment in 1999. He is currently chairman of Fisher & Paykel Appliances and a director of Spark Infrastructure, an Australian listed company. Keith was formerly chairman of Emirates Team New Zealand and deputy chairman of Auckland International Airport. Keith has had an extensive career in electricity, taking part in much of its reform, including the separation of Transpower from Electricity Corporation of New Zealand (ECNZ) in 1992, the separation of Contact Energy from ECNZ in 1996 and the eventual break up of ECNZ into three companies in 1999.



**Mark Ratcliffe**

BA Accounting

Non-Independent Managing Director since 9 December 2011

Mark has been our CEO since our establishment in 2007 as an operationally separate business unit within Telecom and was appointed as our first CEO when we became a separately listed entity in 2011. In a 20 year career with Telecom, Mark held finance, marketing, product development, product management and IT roles. Mark was promoted to the executive team in 1999 where he was CIO (including a period as joint CEO of AAPT in Australia) and then COO Technology and Wholesale before becoming our CEO. From May 2010, he led the team that secured our participation in the Government's UFB initiative and our demerger from Telecom.



**Murray Jordan**

MProp

Independent Director since 1 September 2015  
 Member of Human Resources and Compensation Committee

Murray has extensive experience in the management of highly customer focused organisations and in navigating extremely complex stakeholder environments, including, until recently, as Managing Director of Foodstuffs North Island, one of New Zealand largest companies. Murray has also previously held various general manager positions at Foodstuffs and management roles in the property investment and development sectors. He is a director of Stevenson Group and Metcash Limited, an ASX listed company, and a Board Trustee of Starship Foundation.



**Prue Flacks**

LLB, LLM

Independent Director since 1 December 2011  
 Chairman of Human Resources and Compensation Committee  
 Member of Nominations and Corporate Governance Committee

Prue is a director of Bank of New Zealand and Mercury NZ. She is a barrister and solicitor with extensive experience in commercial law and, in particular, banking, finance and securities law. Her areas of expertise include corporate and regulatory matters, corporate finance, capital markets, securitisation and business restructuring. Prue is a consultant to Russell McVeagh, where she was previously a partner for 20 years.

## Mark Ratcliffe

Chief Executive Officer

See previous page.



## Andrew Carroll, MCA (Hons)

Chief Financial Officer

Andrew joined us after nine years with Telecom where he was involved in a range of corporate finance and M&A activity, including the Gen-i acquisition and the sale of Yellow Pages. He also worked on the UFB negotiations with Crown Fibre Holdings and the demerger process. Prior to joining Telecom he worked in investment banking for a decade.



## Ed Beattie

General Manager, Infrastructure

Ed has more than 30 years' experience in building and maintaining fixed line and mobile telecommunications networks in New Zealand. He managed the delivery of the successful Fibre to the Node programme from 2008 to 2011 and played a lead role in the Christchurch earthquake response and restoration activities. As General Manager Infrastructure, Ed has primary responsibility for the UFB and RBI network rollouts.



## Ewen Powell, BE

Chief Technology Officer

Ewen has over 20 years' experience in managing the technology, services and partnerships that operate a national communications network. He has spent time in both the supplier and operator communities with much of his career spent at Telecom. Ewen's focus is on deploying core enterprise systems to run the business and develop technology capabilities to provision and manage the new fibre network.



## Ian Bonnar

General Manager, Corporate Relations

Ian was appointed General Manager Corporate Relations in October 2014 with overall responsibility for protecting and enhancing our reputation with our stakeholders. Before joining us in 2013 he held a range of positions at Telecom, including Head of Communications, and was communications lead on the UFB negotiations and the demerger process.



## Nick Woodward

General Manager, Customer Service

Nick's career combines a wide range of IT, sales, customer and project management experience in the financial and telecommunications industries. His roles have seen him work across the United States and Europe for Hutchison 3G UK and Household Bank in the United Kingdom.



## Paula Earl-Peacock

General Manager, Human Resources

Paula joined us in November 2014, and has over 20 years' experience in generalist human resources roles in New Zealand and Australia. Her most recent role was in consumer goods with Mars Petcare in Australia. She has also worked in the financial services, consulting and retail sectors. Paula's focus is on the development of high performance organisations through constructive leadership, and the development of people, culture and teams.



## Tim Harris, LLB, MBA

Chief Commercial Officer

Tim joined us in October 2014 as Chief Commercial Officer with responsibility for leading our Marketing, Sales and Corporate Strategy functions. Tim has held a number of senior roles, most recently as Managing Director of BT Global Services South-East Asia. Tim has an MBA from the UK-based Cranfield School of Management.



## Vanessa Oakley, LLB (Hons)

General Counsel & Company Secretary

Vanessa has extensive experience in law, governance and policy and its interaction with commercial operations. She joined us after playing a key role in the UFB contract, legislative and demerger processes. She previously held roles in the public and private sectors, including as a key adviser to United Kingdom and New Zealand regulators and across the Telecom group.



## Irene Lovejoy

Executive Assistant

Irene has worked with CEO Mark Ratcliffe for more than 15 years, bringing a unique insight that adds value to the development of our executive team. Before joining us, Irene spent 22 years with Telecom where she held roles in the marketing, technology and corporate teams.



# Management Commentary

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## Management commentary

	2016 \$M	2015 \$M
Operating revenue	1,008	1,006
Operating expenses	(414)	(404)
<b>Earnings before interest, income tax, depreciation and amortisation</b>	<b>594</b>	<b>602</b>
Depreciation and amortisation	(327)	(324)
<b>Earnings before interest and income tax</b>	<b>267</b>	<b>278</b>
Net interest expense	(140)	(151)
<b>Net earnings before income tax</b>	<b>127</b>	<b>127</b>
Income tax expense	(36)	(36)
<b>Net earnings for the year</b>	<b>91</b>	<b>91</b>

## In summary

We report earnings before interest, income tax, depreciation and amortisation (EBITDA) of \$594 million for the year ending 30 June 2016, a decrease of \$8 million on the prior year. Net earnings have remained unchanged year on year.

Results for the year ending 30 June 2016 (FY16) were affected by the benchmarked Unbundled Bitstream Access (UBA) pricing for about five and a half months of the year and the final aggregate copper pricing determined by the Commission for about six and a half months of the year. Following confirmation that this decision wouldn't be appealed, we progressively reoriented discretionary activity from 'manage for cash' toward 'managing for longer term value'.

Capital expenditure for FY16 was \$593 million. This was at the lower end of the FY16 guidance range of \$580 million to \$630 million and reflects ongoing reductions in communal deployment costs, lower cost to connect and less than estimated demand for 'backbone' fibre connections spend in rights of way premises. About 82% of our capital spend was fibre related, mainly for the UFB and RBI programmes.

We will pay a final dividend of 12 cents per share on 7 October 2016. The dividend reinvestment plan will be available. We expect to pay a dividend of 21 cents per share for FY17, subject to no material adverse changes in circumstance or outlook.



## Revenue commentary

	2016 \$M	2015 \$M
Basic copper	489	491
Enhanced copper	242	268
Fibre	133	98
Value added network services	35	36
Infrastructure	20	21
Field services	83	84
Other	6	8
<b>Total revenue</b>	<b>1,008</b>	<b>1,006</b>

### Revenue overview

Our product portfolio encompasses a broad range of broadband, data and voice wholesale services. It includes a mix of regulated and commercial products. Revenue increased compared to the prior period broadly reflecting the net effect of:

- Changes in regulated copper pricing between the Commission's benchmarking and final pricing review decisions (see the

*Regulation, legislation and litigation* section for more detail);

- A reduction of 67,000 total fixed line connections (from 1,794,000 to 1,727,000); and
- A small increase in broadband connection numbers (from 1,207,000 to 1,226,000).

A summary of our pricing for key copper products is on page 26.

	CONNECTIONS 30 JUN 2016	CONNECTIONS 31 DEC 2015	CONNECTIONS 30 JUN 2015
<b>Total fixed line connections</b>	<b>1,727,000</b>	<b>1,761,000</b>	<b>1,794,000</b>
Baseband copper	1,221,000	1,320,000	1,408,000
UCLL	108,000	116,000	123,000
SLU/SLES	2,000	3,000	3,000
Naked copper (UBA / VDSL)	197,000	180,000	159,000
Baseband IP	9,000	6,000	NM
Data services over copper	10,000	11,000	13,000
Fibre (mass market + premium business)	180,000	125,000	88,000
<b>Total broadband connections</b>	<b>1,226,000</b>	<b>1,223,000</b>	<b>1,207,000</b>
Copper UBA (includes naked UBA)	900,000	972,000	1,016,000
VDSL (includes naked VDSL)	159,000	139,000	116,000
Fibre (mass market)	167,000	112,000	75,000

### Copper

The basic copper category incorporates core regulated products founded on earlier technology and product variants that are being superseded by enhanced copper and fibre-based services. It includes most of Chorus' layer 1 network products such as the copper voice input Unbundled Copper Low Frequency Service (UCLFS), Unbundled Copper Local Loop (UCLL), Sub Loop Unbundling (SLU), Sub Loop Extension Service (SLES) and Basic Unbundled Bitstream Access (Basic UBA) (including broadband only naked Basic UBA connections). Basic copper revenues are declining as customers migrate to these alternative product types.

Enhanced copper includes copper based next generation regulated and commercial products that deliver higher speed capability, a better customer experience and can assist the transition to fibre. It includes Enhanced UBA, VDSL, the Baseband IP voice input service

and High Speed Network Service (HSNS) Lite for business data on copper.

At 30 June 2016, there were approximately 1,221,000 baseband copper lines, a decrease of 187,000 lines from 30 June 2015. This reduction was partially offset by the migration of connections to our other fixed line connection products such as 'naked copper' connections. The number of unbundled lines declined to 110,000. The total comprised 108,000 UCLL lines and 2,000 SLU lines (offered in conjunction with our commercial Sub Loop Extension Service).

Uptake of VDSL continued to grow, up from 116,000 at 30 June 2015 to 159,000 by 30 June 2016 as technology changes expanded the VDSL footprint from 60% to 80% of lines nationwide. 'Data service over copper' connections continued to decline as retail service providers opted for cheaper inputs. Baseband IP connections grew as some retail service providers used the service to deliver their own voice over internet protocol service over copper.

## Revenue commentary (cont.)

### Fibre

Fibre revenues are earned from our business fibre products (such as HSNS Premium) and UFB residential and business fibre services. This includes UFB backhaul and Direct Fibre Access Services, which provide point to point networking solutions and can be used to deliver backhaul connections to mobile sites.

Nationwide fibre connections more than doubled during the year, increasing from 88,000 to 180,000 lines. This was driven by the growing demand for fibre services and the ongoing expansion of the UFB footprint. We had approximately 156,000 fibre connections within the areas where we had deployed UFB communal network at 30 June 2016, up from 68,000 connections at 30 June 2015.

About 167,000 of our fibre connections were to mass market customers (which includes UFB Bitstream 2 and 3 and education connections). Premium fibre connections remained unchanged.

During FY16 there was a marked change in customer uptake with our retail service provider customers promoting 100Mbps plans more heavily than the entry level 30Mbps plan. By 30 June 2016 approximately 54% of mass market fibre connections were on plans of 100Mbps or greater, compared to 32% at the start of the period.

Direct Fibre Access Service connections were about 4,000 of total fibre connections at 30 June 2016. Bandwidth Fibre Access Service and HSNS Premium fibre connections (also referred to as Bitstream 4) accounted for about 7,000 fibre connections. The remaining premium business fibre connections are largely backhaul connections, which are slowly declining over time as network connections are rationalised.

	CONNECTIONS 30 JUN 2016	CONNECTIONS 31 DEC 2015	CONNECTIONS 30 JUN 2015
<b>Total fibre connections</b>	<b>180,000</b>	<b>125,000</b>	<b>88,000</b>
Mass market	167,000	112,000	75,000
Premium business	13,000	13,000	13,000

### Value added network services

The main revenue driver for this category is national data transport services, which provide network connectivity across backhaul links as well as aggregation handover links. Overall value added network services is declining as customers move from legacy backhaul arrangements to new cost effective solutions. There has also been some reduction in backhaul demand due to retail service provider mergers and network consolidation.

### Infrastructure

Infrastructure revenue relates to services that provide access to our network assets, such as renting exchange space. This product revenue is largely flat as declining revenue from larger retail service provider customers investing in their own infrastructure rather than renting ours has offset increased revenue from smaller customers.

### Field services

Field services revenues includes work performed by service company technicians providing new services, chargeable cable location services, maintaining retail service provider networks and relocating our network on request. As we utilise service companies to perform field services work, there is a direct cost associated with all field services revenues recognised in the network maintenance expense category.

We receive provisioning revenues when technicians install services and the revenue is dependent on the number and nature of orders, and the type of work required. Maintenance revenues are generated when faults are on retail service provider's network rather than ours, and depend on the number of reported faults. It is difficult to establish specific trends in this revenue category because it is dependent on third party demand or damages to our network by third parties.

Field Services revenues have remained flat year on year as we are recovering a greater proportion of our costs for greenfields and infill subdivisions, but offsetting this increase are lower regulated transaction charges effective from 16 December 2015.

### Other

Other income largely consists of revenue generated from the provision of billing and network management services to Spark, dividends received from electricity trusts that supply us with electricity and any other minor income.

# Expenditure commentary

## Operating expenses

	2016 \$M	2015 \$M
Labour costs	78	73
Provisioning	60	58
Network maintenance	89	91
Other network costs	34	34
Information technology costs	65	65
Rent and rates	16	14
Property maintenance	12	11
Electricity	14	14
Insurance	3	4
Consultants	4	3
Regulatory levies	13	15
Other	26	22
<b>Total operating expenses</b>	<b>414</b>	<b>404</b>

Operating expenditure has increased by 2.5% relative to FY15. The second half of FY16 has seen a progressive move from 'manage for cash' to 'manage for value'. The focus on a better customer experience has resulted in additional people being employed in the customer services team to more closely manage fibre orders including undertaking activity previously performed by retail service providers. Rent and rates are increasing as our additional network is being incorporated into the local Council rating processes and some property maintenance which had been deferred on our buildings has been completed. Areas of significant change include:

**Labour costs** of \$78 million for the year represent staff costs that are not capitalised. At 30 June 2016 we had 944 permanent and fixed term employees, up from 842 employees at 30 June 2015. We employed 73 more people in the customer services team reflecting the growth in fibre volumes and additional activity we are undertaking to improve the customer experience. These processes are progressively being automated, but are still currently relatively manual and time consuming. The number of people throughout the rest of the business has remained stable throughout the year.

**Provisioning costs** are incurred where we provide new or changed service to our customers. The total provisioning cost is driven by the volume of orders, the type of work required to fulfil them, technician labour, material and overhead costs. Field provisioning costs have declined as fibre uptake increases and fewer truck rolls are required for copper services. The lower truck roll volume is offset by a more expensive unit cost per truck roll as more customers choose VDSL which has historically had a higher cost to provision because it typically required a technician to visit customer premises. In addition, outsourcing costs were incurred for a trial installation support service to manage the customer ordering experience.

**Network maintenance** costs relate to fixing network faults and any operational expenditure arising from the proactive maintenance programme. Where faults are on a retail service provider's network (rather than our network), we will charge the retail service provider for this service. Network maintenance costs are driven by the number of reported faults, the type of work required to fix the faults and the extent of our proactive maintenance programme.

The costs associated with our network reactive faults have fallen by approximately \$2 million with a slight decrease in the both the number of faults and cost per fault. The decrease in faults was partly due to us having lower copper connections and a higher proportion of fibre lines, which have a lower fault rate than copper lines. Partly offsetting this were poorer weather conditions compared to FY15. The average cost per fault has reduced because of a slightly lower proportion of more expensive below ground faults in FY16 compared to FY15.

In addition to the reduction in our network reactive faults there has been a small increase in maintenance on our customers' networks which has been offset by a small reduction in proactive maintenance costs.

**Other network** costs relate to costs associated with service partner contract costs, engineering services, project costs unable to be capitalised and the cost of network spares. Any costs that have been incurred for fibre orders that are subsequently cancelled are included in other network costs. In FY16 there were small increases in the costs of cancelled fibre orders and enhancing fibre network record quality which were offset by reductions in project and service partner contract costs.

## Expenditure commentary (cont.)

**Information technology** costs of \$65 million have remained flat and represent costs paid directly by us to third party vendors for maintenance and support, as well as the operating expenditure component of systems which are shared with Spark. During FY16 we continued work on separating IT systems from Spark which resulted in an increase in expenditure. However, there has been a resulting decrease in systems no longer required, which meant overall costs have remained unchanged from the previous year.

**Rent and rates** costs relate to the operation of our network estate (for example, exchanges, radio sites and roadside cabinets). Rates are levied on network assets both above and below ground. Rent and rates costs have increased during the period as the aerial deployment of fibre has resulted in increased pole rental costs and the assets deployed as part of the UFB rollout being progressively included in the rating calculations of local bodies.

**Property maintenance** costs have increased this year as some maintenance which had been deferred as a result of the initiatives has now been completed.

**Electricity** is used to operate the network electronics and this is dependent on the number of sites, electricity consumption and

electricity prices. Electricity costs have remained largely flat despite increased line charges and additional network related consumption as electricity prices were lower in FY16 than FY15. About 50% of our requirements have been hedged, with a rolling three year horizon.

**Consultant costs** have increased during the current year as projects that had been deferred in the previous year were restarted. In addition we continued to have a significant amount of regulatory work through FY16.

**Regulatory levy** reflects the amount paid for the Telecommunications Development Levy and the Telecommunications Regulation Levy. The expense for the current year reflects the estimated liability for FY16. The FY15 balance reflected the accrual for FY15 as well as a catch up for the difference between the FY13 and FY14 accruals and the final actual costs as these years were finalised during FY15.

**'Other'** includes expenditure on general costs such as advertising, telecommunications, travel, training and legal fees. Overall these costs returned to more typical levels after the tight cost control on discretionary spend since H2 FY15 was eased.

### Depreciation and amortisation

	2016 \$M	2015 \$M	ESTIMATED USEFUL LIFE (YEARS)	WEIGHTED AVERAGE USEFUL LIFE (YEARS)
<b>Depreciation</b>				
Copper cables	56	58	10–30	21
Fibre cables	60	50	20	20
Ducts and manholes	35	31	50	48
Cabinets	41	36	5–14	9
Property	18	17	5–50	25
Network electronics	68	78	2–15	8
Other	-	1	2–10	6
Less: Crown funding	(15)	(12)		
<b>Total depreciation</b>	<b>263</b>	<b>259</b>		
<b>Amortisation</b>				
Software	64	65	2–8	5
Other intangibles	-	-	6–20	20
<b>Total amortisation</b>	<b>64</b>	<b>65</b>		

The weighted average useful life represents the useful life in each category weighted by the net book value of the assets.

During the year ended 30 June 2016 \$593 million of expenditure on network assets and software were capitalised. The 'UFB communal' and 'Fibre connections and fibre layer 2' included in 'fibre' capital expenditure was largely capitalised against the network assets categories of fibre cables (46%) and ducts and manholes (30%). The average depreciation rate for UFB communal infrastructure spend is currently 38 years, reflecting the very high proportion of long life assets being constructed, with ducts and manholes having a depreciation rate of 50 years.

## Net finance expense

	2016 \$M	2015 \$M
<b>Finance income</b>	<b>(7)</b>	<b>(8)</b>
<b>Finance expense</b>		
Interest on syndicated bank facility	60	68
Interest on EMTN	53	53
Interest on fixed rate NZD bonds	3	-
Ineffective portion of change in fair value of cash flow hedge	9	19
Other interest expense	17	19
Capitalised interest	(5)	(6)
<b>Total finance expenses excluding Crown funding</b>	<b>137</b>	<b>153</b>
CFH securities (notional interest)	10	6
<b>Total finance expense</b>	<b>147</b>	<b>159</b>

Interest costs decreased in FY16 largely reflecting the decreased weighted effective interest rate on debt (6.6% in FY16 compared to 6.9% in FY15) as a result of Moody's Investor Services rating upgrade in February 2016 and the impact of lower prevailing market interest rates on floating rate debt. There was also a smaller amount of ineffectiveness arising from change in fair value of cash flow hedge.

We have restructured our debt in the last year, with \$450 million of syndicated bank facility debt being repaid as it came due and replaced with \$400 million of lower cost New Zealand dollar bonds. The NZD bonds were issued on 6 May 2016 with a fixed interest rate of 4.12% and maturity date 6 May 2021. Over time there will be a shift in interest expense from syndicated bank facility to fixed rate NZD bond.

The Euro Medium Term Notes (EMTN) hedging relationship was reset with a fair value of \$49 million on 9 December 2013 following the close out of the interest rate swaps relating to the EMTN. During the current year, ineffectiveness of \$9 million (30 June 2015: \$19 million) flowed through interest expense. A further \$21 million remains in the hedge reserve and will flow as ineffectiveness to interest expense in the income statement at some time over the life of the derivatives. It will be a non-cash charge. Neither the direction, nor the rate of the impact on the income statement can be predicted.

Software and other intangibles largely consist of the software components of billing, provisioning and operational systems, including spend on Spark-owned systems. A total of \$44 million of software was capitalised during the year, which will be amortised over an average of five years.

Our depreciation profile is expected to continue to change, reflecting the greater mix of longer dated assets for the UFB and RBI rollouts. The offset of Crown funding against depreciation is expected to continue to increase over time as the amount of funding received from the Crown accumulates, with the associated amortisation to depreciation increasing accordingly.

Other interest expense includes finance lease interest of \$13 million (30 June 2015: \$13 million), \$1 million of costs relating to the financing tax payments through Tax Management New Zealand and \$3 million amortisation (30 June 2015: \$3 million) arising from the difference between fair value and proceeds realised from the interest rate swap reset.

At a minimum, we aim to maintain 50% of our debt obligations at a fixed rate of interest. We have fully hedged the foreign exchange exposure on the EMTN with cross currency interest rate swaps. The floating interest on these derivatives has been hedged using interest rate swap instruments. The exposure to floating rate interest on the syndicated bank facility has been reduced using interest rate swaps.

As at 30 June 2016, approximately 88% (30 June 2015: 51%) of the outstanding debt obligation was fixed through derivative or fixed rate debt arrangements.

## Taxation

The 2016 effective tax rate of 28% equates to the statutory rate of 28%. There are no material permanent differences between net earnings before income tax and what is, or will be, taxable for the year to 30 June 2016.

## Capital expenditure commentary

	2016 \$M	2015 \$M
Fibre	486	504
Copper	67	60
Common	40	33
<b>Gross capital expenditure</b>	<b>593</b>	<b>597</b>

Gross capital expenditure for the year to 30 June 2016 was \$593 million. This was at the lower end of the FY16 guidance range of \$580 million to \$630 million and reflects ongoing reduction in

communal deployment costs as expected, average connection costs below guidance and less than forecast demand for construction of 'backbone' infrastructure to enable connections in rights of way.

### Fibre capital expenditure

	2016 \$M	2015 \$M
UFB communal	194	236
Fibre connections and fibre layer 2 <sup>1</sup>	205	169
Fibre products and systems	18	26
Other fibre connections and growth <sup>1</sup>	47	34
RBI	22	39
<b>Total fibre capital expenditure</b>	<b>486</b>	<b>504</b>

Fibre capital expenditure includes spend specifically focussed on fibre assets (layer 0 and layer 1 UFB network assets), spend to support the fibre network (IT delivering fibre products) and programmes largely focussed on fibre (UFB and RBI). Fibre capital expenditure represents about 82% of our FY16 gross capital expenditure spend, mainly for the UFB and RBI programmes.

UFB communal network deployment continued to gain momentum with build work completed for about 474,000 premises at 30 June 2016 out of the contractual target of 830,900 premises by the end of 2019. Build work was completed for 106,000 premises during the year.

The cost of the deployment of UFB communal network for the year was \$194 million. This included \$48 million spent on work in progress for communal network scheduled to be completed in the following year, lower than the \$236 million in the previous year.

The average cost per premises passed during the year was \$1,689. This was below FY16 guidance of an average cost of \$1,700 to \$1,770 for the year.

Fibre connections and layer 2 spend was \$205 million as the volume of fibre connections continued to grow in line with our expanding UFB footprint and increasing uptake. Layer 2 equipment, such as Gigabit capable passive optical network ports, was installed ahead of demand as the UFB footprint grew. Demand for higher cost premium business fibre connections was below forecast (2,500 versus 3,500 connections).

The average cost per premises connected for standard residential premises and some non-standard single dwelling unit installations, was \$1,009, excluding the long run average cost of layer 2 equipment. This was below the expected range of \$1,050 to \$1,250, reflecting cheaper actual mix of connection types.

A significant proportion of the fibre connections spend was incurred in providing 'backbone' network to enable the connection of customers located along rights of way or in multi dwelling units. This spend represents upfront investment as it ultimately enables multiple customers in a building, or along a right of way, to connect to UFB. We are able to recover a small proportion of connection costs for particular classes of 'non-standard' connections as defined by the UFB contract with Crown Fibre Holdings (CFH).

Fibre products and systems spend reduced to \$18 million. Key areas of spend included the platform for retail service providers to integrate their fibre ordering with our fibre system, fibre test tools for retail service providers and the online order tracker for customers.

Capital expenditure of \$47 million on other fibre connections and growth reflected new 'greenfield' fibre subdivisions, fibre lifecycle investment and regional backhaul connections for retail service provider data traffic. Transport investment has increased to support broadband capacity and growth and regional transport services on our network.

1 To disclose all connection capex in the same place, premium business fibre capex has been moved to fibre connections and layer 2 capex, previously it was in other fibre connections and growth. FY15 categories have been adjusted for comparative purposes.

The RBI rollout was completed in FY16 with spend of \$22 million, meaning a total cost of \$282 million for the five year programme. This was at the lower end of the initial \$280 – \$295 million range

and we received approximately \$233 million in Government grant funding for the rollout (see the Contributions to capital expenditure section below).

### Copper capital expenditure

	2016 \$M	2015 \$M
Network sustain	29	34
Copper connections	7	11
Copper layer 2	27	11
Product fixed	4	4
<b>Total copper capital expenditure</b>	<b>67</b>	<b>60</b>

Copper capital expenditure was \$67 million for the year, with the increase reflecting further investment in broadband capacity and growth to provide better broadband on our network.

Network sustain expenditure refers to capital expenditure where the network is being upgraded or network elements such as poles, cabinets and cables are replaced. This is typically where there is risk of network failure or degraded service for customers and network replacement is deemed more cost effective than reactive maintenance. As noted during the copper pricing process, proactive maintenance was put on hold and takes time to restart.

Requests to shift network for roadworks purposes continued to increase but the cost is largely recovered in 'Crown Funding – other'.

Capital expenditure on copper connections occurs where there is demand for copper connections for residential or business customers, such as infill housing or new buildings. Demand for copper connections continues to decrease as demand shifts to the UFB network and a contribution for new connections is required.

Copper layer 2 reflects investment in network electronics and equipment as a consequence of demand for broadband capacity and growth. This increased significantly as growing bandwidth demand, driven by online video consumption, required investment in network capacity at some locations.

### Common capital expenditure

	2016 \$M	2015 \$M
Information technology	25	19
Building and engineering services	13	13
Other	2	1
<b>Total common capital expenditure</b>	<b>40</b>	<b>33</b>

Common capital expenditure was \$40 million. Information technology spend increased to \$25 million as we resumed longer term investment following the conclusion of the copper pricing review.

Building and engineering services reflects the capital spent on growth and plant replacement (e.g. power and air conditioning) at our exchanges, buildings and remote sites.

'Other' includes items such as office accommodation and equipment.

### Contributions to capital expenditure

We receive significant financing and contributions towards our gross capital expenditure each year. During the year to 30 June 2016, we received contributions from the following sources:

- i) **RBI funding:** The Crown contributed grant funding of about \$233 million (excluding school lead-in contributions) towards our layer 0 and layer 1 capital spend over the five years of RBI. For the year ended 30 June 2016 \$22 million was recognised.
- ii) **Other:** We are able to recover the cost of other capital spend in certain circumstances. This includes replacing network damaged by third parties, or instances where central or local government authorities ask us to relocate or rebuild existing network. A total of \$6 million was recognised in the current year and is included as part of Crown funding given its modest size.

## Long term capital management

We will pay a final dividend of 12 cents per share on 7 October 2016 to all holders registered at 5.00pm 23 September 2016. The shares will be quoted on an ex-dividend basis from 22 September 2016. The dividends paid will be fully imputed, at a ratio of 28/72, in line with the corporate income tax rate. In addition, a supplementary dividend of 2.12 cents per share will be payable to shareholders who are not resident in New Zealand.

The dividend reinvestment plan will remain in place for the final dividend at a discount rate of 3%. Shareholders who have previously elected to participate in the dividend reinvestment plan do not need to take any further action. For those shareholders who wish to participate, election notices to participate must be received by 5.00pm (NZ time) on 26 September 2016.

During the UFB build programme to 2020, the Board expects to be able to provide shareholders with modest long term dividend growth from the base of 20 cents per share paid in FY16, subject to no material adverse changes in circumstances or outlook.

For FY17, Chorus will pay a dividend of 21.0 cents per share, with an interim dividend of 8.5 cents per share to be paid in April. A final dividend of 12.5 cents per share will be declared in August, subject to no material adverse changes in circumstance or outlook. The dividend reinvestment plan will remain in place for the interim dividend at a discount rate of 3 per cent.

The Board considers that a 'BBB' or equivalent credit rating is appropriate for a company like Chorus. It intends to maintain capital management policies and financial policies consistent with these credit ratings. At 30 June 2016, we had a long term credit rating of BBB/stable outlook by Standard & Poor's and Baa2/stable by Moody's Investors Service.



## Regulation, legislation and litigation

Significant developments in our regulatory environment are set out below. This should be read in conjunction with previous disclosures which are available online at: [www.chorus.co.nz/investor-centre](http://www.chorus.co.nz/investor-centre).

### Chorus Open Access Deeds of Undertaking

We are bound by three open access deeds of undertaking (Deeds). The Copper, Fibre and Rural Broadband Initiative Deeds represent a series of legally binding obligations focused around the provision of services on a non-discriminatory or equivalent basis.

We submitted a transition plan to the Minister for Communications in late 2012 relating to the actions required to move to ending the sharing arrangements between Spark and Chorus, as required by the Deeds. We provide annual updates to the plan, with the most recent update provided in late 2015.

### Telecommunications Services Obligations (TSO) and Levies

The TSO is the regulatory mechanism by which universal service obligations for residential, local access and calling services are imposed and administered. We are required to maintain lines and coverage obligations, and provide a voice input service. On 9 July 2013, the Government issued a discussion document on the TSO, as part of a scheduled review and we made submissions. The timing for a formal update on the review from Government is unknown and there is no guarantee or certainty of the outcome.

The Telecommunications Development Levy (TDL) is an industry levy of \$50 million per year from FY10 and initially scheduled to reduce to \$10 million each year from FY16. In May 2015, the Government extended the TDL so that the levy will continue to be \$50 million per year until FY19, reducing to \$10 million each year thereafter, as part of its RBI extension policy. In December 2015, the Commission determined that we were liable for \$11.1 million of the TDL for FY15.

We are also required to contribute towards the Commission's costs through a Telecommunications Regulatory Levy (TRL). We were liable for \$1.3 million of the TRL for FY15. We may also be required to contribute to the costs of the Commission's regulatory proceedings.

### UCLL and SLU pricing

The terms, including price, for UCLL and SLU are currently regulated by the Commission. In December 2012, the Commission issued a final decision on its benchmarking review of the price we can charge for UCLL. The final averaged UCLL price of \$23.52 represented a 3.8% drop. The UCLL price is linked to a number of our other services, meaning that the UCLFS and SLU prices, and some UBA prices, were impacted by the decision.

We applied to the Commission to review the UCLL price, using a final pricing principle of Total Service Long Run Incremental Cost (TSLRIC). On 15 December 2015, the Commission released a final determination, which proposed a glide path for pricing over a five-year period, the price for the twelve month period from 16 December 2015 is \$29.75 for UCLL and \$15.52 for SLU. In the pending regulatory reviews (refer Regulatory framework review below) the Government is consulting on whether UCLL should remain available after 2020.

### Unbundled Copper Low Frequency Service

To meet our TSO requirements, we have made a technology neutral voice input service, Baseband, available on a commercial basis. The pricing of a subset of this service, UCLFS (a voice input service offered over the copper access network), is set at the averaged UCLL price as determined by the Commission. Because the UCLFS price is linked to the UCLL price, the same UCLL monthly pricing applied to UCLFS from 16 December 2015. The UCLFS price flows contractually to the baseband price.

### UBA pricing

The terms, including price, for UBA are currently regulated by the Commission. The UBA price comprises the UCLL price plus an uplift for UBA. On 5 November 2013, the Commission issued an initial benchmarked decision on the UBA uplift pricing reducing the UBA uplift from \$21.46 to \$10.92 per month based on benchmarking of pricing in two countries. The Commission's initial benchmarked UBA uplift of \$10.92 applied from 1 December 2014.

We applied to the Commission to review the UBA price, using a final pricing principle of TSLRIC. In December 2015, the Commission issued a final determination, with a glide path for the UBA uplift over a five-year period, the price for the 12 month period from 16 December 2015 is \$11.44.

### UBA non-price terms review

The Commission is considering possible changes to the general terms and service description (i.e. regarding the technical characteristics) of the UBA service. A final decision on any changes is expected in late 2016.

## Regulation, legislation and litigation (cont.)

### Regulatory framework review

Under amendments made to the Telecommunications Act to facilitate Chorus' demerger, the Government was required to commence a review of the regulatory framework by 2016, with a particular focus on the framework to apply once the UFB build is complete in 2020.

On 8 September 2015, the Government released a discussion document that stated: "A predictable, proportionate and flexible regulatory framework for communications will enable competition, innovation, investment, and growth across the economy which ultimately is better for consumers." The discussion document acknowledged that structural separation means wholesale-only fixed line providers including Chorus appear more like electricity lines businesses, which are subject to "utility-style" regulation.

The document's "preliminary view" was that a building block model (BBM) is the most appropriate framework for regulating UFB services because: "BBM will promote the legitimate commercial interests of access providers and access seekers and should provide a suitable basis for robust retail competition over the UFB network. BBM will limit the ability of UFB suppliers to generate excess profits, while also providing the stability and incentives needed to encourage efficient investment post-2020." Chorus and other industry participants provided submissions on the discussion document in late October 2015.

On 14 April 2016 the Government announced a series of high-level policy decisions that included:

- Moving to a utility-style model for regulating both fixed line copper and fibre wholesale services;
- The utility-style model could include anchor products for basic voice and basic broadband with reference to entry level prices in the market; and
- Retaining the current fibre unbundling requirements on the UFB network from 2020.

This was followed by the release of a second discussion document in July 2016. The options paper confirms a need for change and supports utilities regulation using a BBM for Chorus' copper and fibre access services and for other UFB fixed line network providers.

The options paper seeks feedback on a proposed BBM design that includes:

- a revenue cap approach;
- two categories of regulated services (anchor products for voice, entry level and basic broadband that have price and quality determined, and commercial services set by a UFB provider subject to minimum requirements); and
- the continuation of nationally averaged pricing.

Other proposals include reinforcement of a consumer led migration to UFB services and discussion regarding price and revenue transition risks and options.

Legislation is proposed to be passed in 2017 followed by substantial regulatory processes to implement the framework akin to the regulatory processes for other utilities in New Zealand.

### Consenting requirements

The Telecommunications (Property Access and Other Matters) Bill was introduced to Parliament on 29 June 2016. The Bill proposes to introduce streamlined consenting processes to make it easier for Chorus to install fibre where the consent of more than one party is required. The Bill received multiparty support at its first reading. The timing and outcome of any consequential law changes is not known.

### Other legislation

Chorus is subject to other legislative requirements such as the requirements of the Commerce Act 1986, Fair Trading Act 1986, as well as telecommunications codes.

Chorus is also subject to the Telecommunications (Interception Capability and Security) Act 2013 (TICSA), which replaces the Telecommunications (Interception Capability) Act 2004. The TICSA has reduced Chorus' obligations to provide lawful interception capability as Chorus is no longer required to pre-invest in lawful interception solutions for wholesale network services and infrastructure level services.

However, the TICSA introduced new obligations on network operators to prevent, sufficiently mitigate or remove network security risks arising from public telecommunications networks. Chorus, like other network operators, is obliged to engage with the Government Communications Security Bureau where it might affect New Zealand's national security and this has the potential to drive significant compliance costs.

### Litigation

We have ongoing claims, investigations and inquiries, none of which are currently expected to have significant effect on our financial position or profitability.

We cannot reasonably estimate the adverse effect, if any, of the outstanding matters are ultimately resolved against our interest. There can be no assurance that such cases will not have a significant effect on our business, financial position, and results of operations or profitability.

# Appendix one

## Non statutory measure: adjusted EBITDA

This appendix provides a high level summary of Chorus' adjusted EBITDA. It has been prepared on the basis of the final pricing principle (FPP) determinations effective 16 December 2015.

For comparative purposes this flows the pricing through both FY15 and FY16 as though the pricing had changed on 1 July 2014.

### Summary

	ADJUSTED 2016 \$M	ADJUSTED 2015 \$M	%
Adjusted operating revenue	1,067	1,073	(0.6)
Operating expenses	(414)	(404)	(2.5)
<b>Adjusted EBITDA</b>	<b>653</b>	<b>669</b>	<b>(2.4)</b>

### Adjusted operating revenue

	STATUTORY RESULTS \$M	ADD: UBA AND UCLL PRICE CHANGE \$M	LESS: TRANSACTION CHARGE PRICE CHANGE \$M	ADJUSTED \$M
H2 FY16 operating revenue	529	-	-	529
H1 FY16 operating revenue	479	65	(6)	538
H2 FY15 operating revenue	479	67	(6)	540
H1 FY15 operating revenue	527	8	(2)	533

## Appendix two

### Copper price paths

#### Copper pricing

	BENCHMARK PRICING	PRICING EFFECTIVE 16 DECEMBER 2015
UCLL and UCLFS	\$23.52	Year 1 – \$29.75
		Year 2 – \$30.22
		Year 3 – \$30.70
		Year 4 – \$31.19
		Year 5 – \$31.68
Basic UBA uplift	\$10.92	Year 1 – \$11.44
		Year 2 – \$11.22
		Year 3 – \$11.01
		Year 4 – \$10.83
		Year 5 – \$10.67
UCLL + UBA = aggregate Basic UBA price	\$34.44	Year 1 – \$41.19
		Year 2 – \$41.44
		Year 3 – \$41.71
		Year 4 – \$42.02
		Year 5 – \$42.35
SLU	\$14.21	Year 1 – \$15.52
		Year 2 – \$15.70
		Year 3 – \$15.89
		Year 4 – \$16.07
		Year 5 – \$16.26



# Financial Statements

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# Independent auditor's report

## To the shareholders of Chorus Limited

### Report on the audit of the Consolidated Financial Statements

#### Opinion

We have audited the consolidated financial statements of Chorus Limited (the Company) and its subsidiary (the Group), which comprise the consolidated statement of financial position as at 30 June 2016, the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Group as at 30 June 2016, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS) and International Financial Reporting Standards (IFRS).

This report is made solely to the shareholders as a body. Our audit work has been undertaken so that we might state to the Company's shareholders those matters we are required to state to them in the auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company's shareholders as a body, for our audit work, this report or any of the opinions we have formed.

#### Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (New Zealand) (ISAs (NZ)). Our responsibilities under those standards are further described in the Auditor's Responsibilities section of our report. We are independent of the Group in accordance with the Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our firm has also provided regulatory audit services, other assurance services, tax compliance services and sponsorship services to the Company and Group. Subject to certain restrictions, partners and employees of our Firm may also deal with the Group on normal terms within the ordinary course of trading activities of the business of the Group. These matters have not impaired our independence as auditor of the Group. The firm has no other relationship with, or interest in, the Group.

#### Audit materiality

The scope of our audit was influenced by our application of materiality. Materiality helped us to determine the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the consolidated financial statements as a whole. The materiality for the consolidated financial statements as a whole was set at \$8,680,000, determined with reference to a benchmark of Group profit before tax as disclosed in the consolidated income statement. We chose profit before tax on the basis that we believe it is the benchmark against which the performance of the Group is commonly measured. Materiality represents 5% of the benchmark.

#### Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements in the current period. We summarise below those matters, our key audit procedures to address those matters and our findings from those procedures in order that the Group's shareholders as a body may better understand the process by which we arrived at our audit opinion. Our findings are the result of procedures undertaken in the context of and solely for the purpose of our statutory audit opinion on the consolidated financial statements as a whole and we do not express discrete opinions on separate elements of the consolidated financial statements.



KEY AUDIT MATTER	OUR PROCEDURES TO ADDRESS THE KEY AUDIT MATTER AND FINDINGS
<p><b>Capitalisation and asset lives</b></p> <p>As disclosed in note 1 of the financial statements, the Group has network assets of \$3,656 million (30 June 2015: \$3,406 million).</p> <p>Capitalisation of costs and useful lives assigned to these assets are a key audit matter due to the significance of assets to the Group's consolidated statement of financial position, and due to the judgement involved in the:</p> <ul style="list-style-type: none"> <li>• decision to capitalise or expense costs;</li> <li>• estimation of the stage of completion of assets under construction; and</li> <li>• estimation of the useful life of the asset once the costs are capitalised.</li> </ul>	<p>Our procedures included:</p> <ul style="list-style-type: none"> <li>• Examining the operating effectiveness of controls around the settlement of capital projects into the fixed asset register and the approval of the asset life annual review.</li> <li>• Assessing the nature of costs incurred in capital projects by checking a sample of costs to invoice to determine whether the description of the expenditure met the capitalisation criteria.</li> <li>• Evaluating a sample of assets under construction in which no costs had been incurred in the final three months of the financial reporting period. We challenged the status of those assets under construction to determine whether they remained appropriately capitalised.</li> <li>• Assessing, on a sample basis, whether the accruals recorded for assets under construction were calculated in accordance with the progress of construction and the arrangements with external suppliers.</li> <li>• Assessing the useful economic lives of the assets, by comparing to industry benchmarks and our knowledge of the business and its operations.</li> </ul>
<p><b>CFH securities and derivative financial instruments</b></p> <p>As disclosed in notes 3, 4, 5 and 18 of the financial statements, the Group has external loans of \$1,540 million (30 June 2015: \$1,663 million), crown funding of \$639 million (30 June 2015: \$523 million) and derivative financial instruments of \$214 million (30 June 2015: \$56 million).</p> <p>The CFH securities and interest rate derivatives are a key audit matter due to their significance to the Group's consolidated statement of financial position. There is complexity and judgement involved in determining the appropriate valuation and accounting treatment for the interest rate derivatives and the CFH securities.</p>	<p>Our procedures included:</p> <ul style="list-style-type: none"> <li>• Assessing the valuation of the interest rate derivatives. Our financial instrument specialists re-valued all interest rate derivatives using valuation models and inputs independent from those utilised by management.</li> <li>• Evaluating the hedge effectiveness of the interest rate derivatives hedging the Euro Medium Term Notes. Our financial instrument specialists assessed the effectiveness of these hedges by independently modelling the future changes in the value of these instruments to assess whether the underlying interest rate derivatives were effective.</li> <li>• Assessing the accounting treatment of the CFH securities. We read the underlying loan agreement and analysed the various features of the loan agreement to determine whether the CFH securities were a debt or equity instrument.</li> <li>• Evaluating the valuation of the CFH securities. Our valuation specialists assessed the methodology used by management for determining the amounts allocated to debt and government grant.</li> <li>• Assessing the inputs used in the valuation of the CFH securities. On a sample basis we compared interest rates and credit spreads to independent sources of information to determine an acceptable range of valuation inputs.</li> </ul>
<p><b>Accuracy of revenue</b></p> <p>As disclosed in note 7 of the consolidated financial statements, the Group has revenue of \$1,008 million (30 June 2015: \$1,006 million).</p> <p>Accuracy of revenue is considered to be a key audit matter due to the nature of the underlying billing processes that existed following the Chorus demerger from Spark New Zealand in 2011.</p> <p>There are certain legacy products where the billing is based on network consumption which cannot be easily linked to a physical end user connection. There is a risk that revenue billed on this basis may be disputed by Chorus' customers who have a different view of their consumption of the Chorus network. Due to the legacy nature of these products, the volumes are decreasing each year and are approximately 20% of revenue in the current financial year.</p>	<p>Our procedures included:</p> <ul style="list-style-type: none"> <li>• Evaluating the Group's recognition of revenue by assessing any revenue disputes recorded in the industry's dispute reporting tool by Chorus customers. We compared the disputes raised by Chorus customers to the revenue recorded by Chorus and checked a sample of settled disputes to the final settlement agreements.</li> <li>• Independently confirming the accuracy of a sample of outstanding debtor balances with Chorus customers.</li> <li>• Agreeing a sample of revenue adjustments recorded during the year to authorised credit notes.</li> </ul>



#### Information other than the Consolidated Financial Statements and Auditor's Report

The directors are responsible for all other information included in an entity's Annual Report. Other information may include the Chairman's report, CEO's Report, disclosures relating to corporate governance and statutory information. Our opinion on the consolidated financial statements does not cover any other information and we will not express any form of audit opinion or assurance conclusion thereon.

In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

#### Directors' Responsibilities for the Consolidated Financial Statements

The directors are responsible on behalf of the entity for the preparation and fair presentation of the consolidated financial statements in accordance with NZ IFRS, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors are responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

#### Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (NZ) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

A detailed description of the auditors' responsibilities including those related to assessment of risk of material misstatement, evaluation of appropriateness of going concern assumptions and determining key audit matters are available on the External Reporting Board website: [https://www.xrb.govt.nz/Site/Auditing\\_Assurance\\_Standards/Current\\_Standards/Page1.aspx](https://www.xrb.govt.nz/Site/Auditing_Assurance_Standards/Current_Standards/Page1.aspx)

**Brent Manning**  
Partner

For and on behalf of KPMG, Wellington  
29 August 2016



# Income statement

FOR THE YEAR ENDED 30 JUNE 2016

(DOLLARS IN MILLIONS)	NOTES	2016 \$M	2015 \$M
Operating revenue	7	1,008	1,006
Operating expenses	8	(414)	(404)
<b>Earnings before interest, income tax, depreciation and amortisation</b>		<b>594</b>	<b>602</b>
Depreciation	1	(263)	(259)
Amortisation	2	(64)	(65)
<b>Earnings before interest and income tax</b>		<b>267</b>	<b>278</b>
Finance income		7	8
Finance expense	3	(147)	(159)
<b>Net earnings before income tax</b>		<b>127</b>	<b>127</b>
Income tax expense	12	(36)	(36)
<b>Net earnings for the year</b>		<b>91</b>	<b>91</b>
<b>Earnings per share</b>			
Basic earnings per share (dollars)	16	0.23	0.23
Diluted earnings per share (dollars)	16	0.19	0.19

# Statement of comprehensive income

FOR THE YEAR ENDED 30 JUNE 2016

(DOLLARS IN MILLIONS)	NOTE	2016 \$M	2015 \$M
<b>Net earnings for the year</b>		<b>91</b>	<b>91</b>
<b>Other comprehensive income</b>			
<b>Items that will be reclassified subsequently to income statement when specific conditions are met</b>			
Ineffective portion of changes in fair value of cash flow hedges	15	7	14
Effective portion of changes in fair value of cash flow hedges	15	(29)	(16)
Amortisation of de-designated cash flow hedges transferred to income statement	15	(1)	(1)
<b>Other comprehensive income net of tax</b>		<b>(23)</b>	<b>(3)</b>
<b>Total comprehensive income for the year net of tax</b>		<b>68</b>	<b>88</b>

The accompanying notes are an integral part of these financial statements

# Statement of financial position

AS AT 30 JUNE 2016

(DOLLARS IN MILLIONS)	NOTES	2016 \$M	2015 \$M
<b>Current assets</b>			
Cash and call deposits	13	102	80
Income tax receivable	12	3	-
Trade and other receivables	9	158	165
Derivative financial instruments	18	1	3
Finance lease receivable	14	4	3
<b>Total current assets</b>		<b>268</b>	<b>251</b>
<b>Non-current assets</b>			
Derivative financial instruments	18	-	14
Trade and other receivables	9	10	11
Software and other intangibles	2	160	159
Network assets	1	3,656	3,406
<b>Total non-current assets</b>		<b>3,826</b>	<b>3,590</b>
<b>Total assets</b>		<b>4,094</b>	<b>3,841</b>
<b>Current liabilities</b>			
Trade and other payables	10	347	315
Income tax payable	12	-	12
Derivative financial instruments	18	24	12
<b>Total current liabilities excluding Crown funding</b>		<b>371</b>	<b>339</b>
Current portion of Crown funding	5	17	13
<b>Total current liabilities</b>		<b>388</b>	<b>352</b>
<b>Non-current liabilities</b>			
Derivative financial instruments	18	191	61
Finance lease payable	14	136	130
Debt	3	1,540	1,663
Deferred tax payable	12	194	199
<b>Total non-current liabilities excluding CFH securities and Crown funding</b>		<b>2,061</b>	<b>2,053</b>
CFH securities	4	152	107
Crown funding	5	622	510
<b>Total non-current liabilities</b>		<b>2,835</b>	<b>2,670</b>
<b>Total liabilities</b>		<b>3,223</b>	<b>3,022</b>
<b>Equity</b>			
Share capital	15	481	465
Reserves	15	(26)	(3)
Retained earnings		416	357
<b>Total equity</b>		<b>871</b>	<b>819</b>
<b>Total liabilities and equity</b>		<b>4,094</b>	<b>3,841</b>

The accompanying notes are an integral part of these financial statements

On behalf of the Board



Patrick Strange, Chairman

Authorised for issue on 29 August 2016



Mark Ratcliffe, Managing Director

# Statement of changes in equity

FOR THE YEAR ENDED 30 JUNE 2016

(DOLLARS IN MILLIONS)	NOTE	SHARE CAPITAL \$M	RETAINED EARNINGS \$M	CASH FLOW HEDGE RESERVE \$M	TOTAL \$M
<b>Balance at 1 July 2014</b>		<b>465</b>	<b>266</b>	<b>-</b>	<b>731</b>
<b>Comprehensive income</b>					
Net earnings for the year		-	91	-	91
<b>Other comprehensive income</b>					
Ineffective portion of changes in fair value of cash flow hedges	15	-	-	14	14
Effective portion of changes in fair value of cash flow hedges	15	-	-	(16)	(16)
Amortisation of de-designated cash flow hedges transferred to income statement	15	-	-	(1)	(1)
<b>Total comprehensive income</b>		<b>-</b>	<b>91</b>	<b>(3)</b>	<b>88</b>
<b>Balance at 30 June 2015</b>		<b>465</b>	<b>357</b>	<b>(3)</b>	<b>819</b>
<b>Comprehensive income</b>					
Net earnings for the year		-	91	-	91
<b>Other comprehensive income</b>					
Ineffective portion of changes in fair value of cash flow hedges	15	-	-	7	7
Effective portion of changes in fair value of cash flow hedges	15	-	-	(29)	(29)
Amortisation of de-designated cash flow hedges transferred to income statement	15	-	-	(1)	(1)
<b>Total comprehensive income</b>		<b>-</b>	<b>91</b>	<b>(23)</b>	<b>68</b>
<b>Contributions by and (distributions to) owners:</b>					
Dividends	15	-	(32)	-	(32)
Supplementary dividends		-	3	-	3
Tax credit on supplementary dividends		-	(3)	-	(3)
Dividend reinvestment plan	15	17	-	-	17
Employee share plan	15	(1)	-	-	(1)
<b>Total transactions with owners</b>		<b>16</b>	<b>(32)</b>	<b>-</b>	<b>(16)</b>
<b>Balance at 30 June 2016</b>		<b>481</b>	<b>416</b>	<b>(26)</b>	<b>871</b>

The accompanying notes are an integral part of these financial statements

# Statement of cash flows

FOR THE YEAR ENDED 30 JUNE 2016

(DOLLARS IN MILLIONS)	NOTES	2016 \$M	2015 \$M
<b>Cash flows from operating activities</b>			
Cash was provided from/(applied to):			
Cash received from customers		1,003	1,006
Finance income		3	4
Payment to suppliers and employees		(404)	(414)
Taxation paid	12	(47)	(48)
Interest paid		(120)	(132)
<b>Net cash flows from operating activities</b>		<b>435</b>	<b>416</b>
<b>Cash flows applied to investing activities</b>			
Cash was applied to:			
Purchase of network assets and software and intangible assets		(569)	(589)
Capitalised interest paid		(5)	(6)
<b>Net cash flows applied to investing activities</b>		<b>(574)</b>	<b>(595)</b>
<b>Cash flows from financing activities</b>			
Cash was provided from/(applied to):			
Net proceeds from finance leases		5	3
Crown funding (including CFH securities)		179	155
Proceeds from debt		585	63
Repayment of debt		(593)	(138)
Dividends paid		(15)	-
<b>Net cash flows from financing activities</b>		<b>161</b>	<b>83</b>
<b>Net cash flow</b>		<b>22</b>	<b>(96)</b>
Cash at the beginning of the year		80	176
<b>Cash at the end of the year</b>	13	<b>102</b>	<b>80</b>

The accompanying notes are an integral part of these financial statements

## Statement of cash flows (cont.)

### RECONCILIATION OF NET EARNINGS TO NET CASH FLOWS FROM OPERATING ACTIVITIES

(DOLLARS IN MILLIONS)	2016 \$M	2015 \$M
Net earnings for the year	91	91
<i>Adjustment for:</i>		
Depreciation charged on network assets	278	271
Amortisation of Crown funding	(15)	(12)
Amortisation of software and other intangible assets	64	65
Deferred income tax	4	8
Ineffective portion of changes in fair value of cash flow hedges (pre-tax)	9	19
Other	11	2
	<b>442</b>	<b>444</b>
<i>Change in current assets and liabilities:</i>		
Change in trade and other receivables	(11)	(16)
Change in trade and other payables	19	8
Change in income tax receivable	(15)	(20)
	<b>(7)</b>	<b>(28)</b>
<b>Net cash flows from operating activities</b>	<b>435</b>	<b>416</b>

The accompanying notes are an integral part of these financial statements

# Notes to the financial statements

Chorus includes Chorus Limited together with its subsidiaries.

Chorus is New Zealand's largest fixed line communications infrastructure services provider, it maintains and builds a network predominantly made up of local telephone exchanges, cabinets, copper and fibre cables.

Chorus Limited is a profit-orientated company registered in New Zealand under the Companies Act 1993 and a FMC Reporting Entity for the purposes of the Financial Markets Conduct Act 2013. Chorus Limited was established as a standalone, publicly listed entity on 1 December 2011, upon its demerger from Telecom Corporation of New Zealand Limited (Telecom), now known as Spark New Zealand Limited (Spark). The demerger was a condition of an agreement with CFH to enable Chorus Limited to be the Crown's UFB provider in 24 regions, representing approximately 70% of the UFB coverage area. Chorus Limited is listed and its ordinary shares quoted on the NZX main board equity security market (NZX Main Board) and on the Australian Stock Exchange (ASX) and has bonds quoted on the NZX debt market. American Depositary Shares, each representing five ordinary shares (and evidenced by American Depositary Receipts), are not listed but are traded on the over-the-counter market in the United States.

These financial statements have been prepared in accordance with generally accepted accounting practice in New Zealand (NZ GAAP) and the Financial Reporting Act 2013. They comply with New Zealand equivalents to International Financial Reporting Standards (NZ IFRS) as appropriate for profit-oriented entities, and with International Financial Reporting Standards.

These financial statements are expressed in New Zealand dollars. All financial information has been rounded to the nearest million, unless otherwise stated.

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

## Accounting policies and standards

Accounting policies that summarise the measurement basis used and are relevant to the understanding of the financial statements are provided throughout the accompanying notes.

The accounting policies adopted have been applied consistently throughout the periods presented in these financial statements. Certain comparative information has been reclassified to conform with the current year's presentation.

There are no new standards, amendments or interpretations that have been issued and effective, that are expected to have a significant impact.

## Accounting estimates and judgements

In preparing the financial statements management has made estimates and assumptions about the future that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

Estimates and assumptions are regularly evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The principal areas of judgement in preparing these financial statements are set out below.

### Network assets (note 1)

Assessing the appropriateness of useful life and residual value estimates of network assets requires a number of factors to be considered such as the physical condition of the asset, expected period of use of the asset, technological advances, regulation and expected disposal proceeds from the future sale of the asset.

### CFH securities (note 4)

Determining the fair value of the CFH securities requires assumptions on expected future cash flows and discount rates based on future long dated swap curves.

### Crown funding (note 5)

Exercising judgement when recognising Crown funding to determine if conditions of the funding contract have been satisfied. This judgement will be based on the facts and circumstances that are evident for each contract at the time of preparing the financial statements.

### Leases (note 14)

Determining whether a lease agreement is a finance lease or operating lease requires judgement as to whether the agreement transfers substantially all the risks and rewards of ownership to Chorus.

### Financial risk management (note 19)

Credit valuations adjusting to reflect credit risk as required by NZ IFRS 13: Fair Value Measurement. The effect of credit risk is quantified using an expected future exposure methodology where credit default swap prices are used to represent the probability of default.

## Note 1 – Network assets

In the statement of financial position, network assets are stated at cost less accumulated depreciation and any accumulated impairment losses. The cost of additions to network assets and work in progress constructed by Chorus includes the cost of all materials used in construction, direct labour costs specifically associated with construction, interest costs that are attributable to the asset, resource management consent costs and attributable overheads.

Repairs and maintenance costs are recognised in the income statement as incurred.

### Estimating useful lives and residual values of network assets

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

Where an item of network assets comprises major components having different useful lives, the components are accounted for as separate items of network assets.

## Note 1 – Network assets (cont.)

Where the remaining useful lives or recoverable values have diminished due to technological, regulatory or market condition changes, depreciation is accelerated. The asset's residual values, useful lives, and methods of depreciation are reviewed annually and adjusted prospectively, if appropriate.

Depreciation is charged on a straight-line basis to write down the cost of network assets to its estimated residual value over its estimated useful life. Estimated useful lives are as follows:

Copper cables	10-30 years
Fibre cables	20 years
Ducts and manholes	50 years
Cabinets	5-14 years
Property	5-50 years
Network electronics	2-15 years
Other	2-10 years

Other network assets include motor vehicles, network management and administration systems and radio infrastructure.

Any future adverse impacts arising when assessing the carrying value or lives of network assets could lead to future impairment losses or increases in depreciation charges that could affect future earnings.

An item of network assets and any significant part is derecognised upon disposal or when no future economic benefits are expected from its use or disposal. Where network assets are disposed of, the profit or loss recognised in the income statement is calculated as the difference between the sale price and the carrying value of the asset.

Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rates as at the dates of the initial transactions.

Land and work in progress are not depreciated.

AS AT 30 JUNE 2016	COPPER CABLES \$M	FIBRE CABLES \$M	DUCTS AND MANHOLES \$M	CABINETS \$M	PROPERTY \$M	NETWORK ELECTRONICS \$M	OTHER \$M	WORK IN PROGRESS \$M	TOTAL \$M
<b>Cost</b>									
Balance as at 1 July 2015	2,333	1,136	1,690	485	521	1,559	4	87	7,815
Additions	-	-	-	-	-	-	-	528	528
Disposals	-	-	-	-	-	-	(1)	-	(1)
Transfers from work in progress	20	200	145	52	19	79	1	(516)	-
<b>Balance as at 30 June 2016</b>	<b>2,353</b>	<b>1,336</b>	<b>1,835</b>	<b>537</b>	<b>540</b>	<b>1,638</b>	<b>4</b>	<b>99</b>	<b>8,342</b>
<b>Accumulated depreciation</b>									
Balance as at 1 July 2015	(1,774)	(328)	(441)	(270)	(232)	(1,361)	(3)	-	(4,409)
Depreciation	(56)	(60)	(35)	(41)	(18)	(68)	-	-	(278)
Disposals	-	-	-	-	-	-	1	-	1
<b>Balance as at 30 June 2016</b>	<b>(1,830)</b>	<b>(388)</b>	<b>(476)</b>	<b>(311)</b>	<b>(250)</b>	<b>(1,429)</b>	<b>(2)</b>	<b>-</b>	<b>(4,686)</b>
<b>Net carrying amount</b>	<b>523</b>	<b>948</b>	<b>1,359</b>	<b>226</b>	<b>290</b>	<b>209</b>	<b>2</b>	<b>99</b>	<b>3,656</b>

AS AT 30 JUNE 2015	COPPER CABLES \$M	FIBRE CABLES \$M	DUCTS AND MANHOLES \$M	CABINETS \$M	PROPERTY \$M	NETWORK ELECTRONICS \$M	OTHER \$M	WORK IN PROGRESS \$M	TOTAL \$M
<b>Cost</b>									
Balance as at 1 July 2014	2,307	956	1,427	444	507	1,519	4	103	7,267
Additions	-	-	-	-	-	-	-	547	547
Other	-	-	-	-	-	-	-	2	2
Disposals	-	-	-	-	-	(1)	-	-	(1)
Transfers from work in progress	26	180	263	41	14	41	-	(565)	-
<b>Balance as at 30 June 2015</b>	<b>2,333</b>	<b>1,136</b>	<b>1,690</b>	<b>485</b>	<b>521</b>	<b>1,559</b>	<b>4</b>	<b>87</b>	<b>7,815</b>
<b>Accumulated depreciation</b>									
Balance as at 1 July 2014	(1,716)	(278)	(410)	(234)	(215)	(1,284)	(2)	-	(4,139)
Depreciation	(58)	(50)	(31)	(36)	(17)	(78)	(1)	-	(271)
Disposals	-	-	-	-	-	1	-	-	1
<b>Balance as at 30 June 2015</b>	<b>(1,774)</b>	<b>(328)</b>	<b>(441)</b>	<b>(270)</b>	<b>(232)</b>	<b>(1,361)</b>	<b>(3)</b>	<b>-</b>	<b>(4,409)</b>
<b>Net carrying amount</b>	<b>559</b>	<b>808</b>	<b>1,249</b>	<b>215</b>	<b>289</b>	<b>198</b>	<b>1</b>	<b>87</b>	<b>3,406</b>

## Note 1 – Network assets (cont.)

There are no restrictions on our network assets or any network assets pledged as securities for liabilities. At 30 June 2016 the contractual commitment for acquisition and construction of network assets was \$341 million (30 June 2015: \$448 million).

### Depreciation

	2016 \$M	2015 \$M
Depreciation charged on network assets	278	271
Less: Crown funding – Ultra-Fast Broadband	(8)	(6)
Crown funding – Rural Broadband Initiative	(6)	(4)
Crown funding – Other	(1)	(2)
<b>Total depreciation</b>	<b>263</b>	<b>259</b>

Chorus receives funding from the Crown to finance the capital expenditure associated with the development of the UFB network, rural broadband services and other services. Funding is offset against depreciation over the life of the assets the funding is used to construct.

Refer to note 5 for information on Crown funding.

### Property exchanges

Chorus has leased property exchange space owned by Spark subject to finance lease arrangements. These have been included in network assets under the property category. As at 30 June 2016 the property exchange assets capitalised under a finance lease had a cost of \$162 million (30 June 2015: \$157 million) together with accumulated depreciation of \$21 million (30 June 2015: \$16 million).

### Impairment

The carrying amounts of non-financial assets including network assets, software and other intangibles are reviewed at the end of each reporting period for any indicators of impairment. If any such indication exists, the recoverable amount of the asset is estimated. An impairment loss is recognised in earnings whenever the carrying amount of an asset exceeds its estimated recoverable amount. Should the conditions that gave rise to the impairment loss no longer exist, and the assets are no longer considered to be impaired, a reversal of an impairment loss would be recognised immediately in earnings.

The recoverable amount is the greater of an asset's value in use and fair value less costs to sell. Chorus' assets do not generate independent cash flows and are therefore assessed from a single cash-generating unit perspective. In assessing the recoverable amount, the estimates of future cash flows are discounted to their net present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the business.

During the year ended 30 June 2016 there was no impairment loss on the network assets or software and other intangibles (30 June 2015: nil).

### Capitalised interest

Finance costs are capitalised on qualifying items of network assets and software assets at an annualised rate of 6.50% (30 June 2015: 6.50%). Interest is capitalised over the period required to complete the assets and prepare them for their intended use. In the current year finance costs totalling \$5 million (30 June 2015: \$6 million) have been capitalised against network assets and software assets.



## Note 2 – Software and other intangibles

Software and other intangible assets are initially measured at cost. The direct costs associated with the development of network and business software for internal use are capitalised where project success is probable and the capitalisation criteria is met. Following initial recognition, software and other intangible assets are stated at cost less accumulated amortisation and impairment losses. Software and other intangible assets with a finite life are amortised from the date the asset is ready for use on a straight-line basis over its estimated useful life which is as follows:

Software	2-8 years
Other intangibles	6-20 years

Other intangibles mainly consist of land easements.

At each reporting date, Chorus reviews the carrying amounts of its software and other intangible assets to determine whether there is any indication that those assets have suffered an impairment loss. For impairment policy and process refer to note 1.

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

There are no restrictions on software and other intangible assets or any software and other intangible assets pledged as securities for liabilities. At 30 June 2016 the contractual commitment for acquisition of software and other intangible assets was \$6 million (30 June 2015: \$4 million).

AS AT 30 JUNE 2016	SOFTWARE \$M	OTHER INTANGIBLES \$M	WORK IN PROGRESS \$M	TOTAL \$M
<b>Cost</b>				
Balance as at 1 July 2015	553	6	10	569
Additions	-	-	65	65
Transfers from work in progress	44	-	(44)	-
<b>Balance as at 30 June 2016</b>	<b>597</b>	<b>6</b>	<b>31</b>	<b>634</b>
<b>Accumulated amortisation</b>				
Balance as at 1 July 2015	(409)	(1)	-	(410)
Amortisation	(64)	-	-	(64)
<b>Balance as at 30 June 2016</b>	<b>(473)</b>	<b>(1)</b>	<b>-</b>	<b>(474)</b>
<b>Net carrying amount</b>	<b>124</b>	<b>5</b>	<b>31</b>	<b>160</b>

AS AT 30 JUNE 2015	SOFTWARE \$M	OTHER INTANGIBLES \$M	WORK IN PROGRESS \$M	TOTAL \$M
<b>Cost</b>				
Balance as at 1 July 2014	467	6	46	519
Additions	-	-	50	50
Transfers from work in progress	86	-	(86)	-
<b>Balance as at 30 June 2015</b>	<b>553</b>	<b>6</b>	<b>10</b>	<b>569</b>
<b>Accumulated amortisation</b>				
Balance as at 1 July 2014	(344)	(1)	-	(345)
Amortisation	(65)	-	-	(65)
<b>Balance as at 30 June 2015</b>	<b>(409)</b>	<b>(1)</b>	<b>-</b>	<b>(410)</b>
<b>Net carrying amount</b>	<b>144</b>	<b>5</b>	<b>10</b>	<b>159</b>

### Note 3 – Debt

Debt is included as non-current liabilities except for those with maturities less than 12 months from the reporting date, which are classified as current liabilities.

Debt is initially measured at fair value, less any transaction costs that are directly attributable to the issue of the instruments.

Debt is subsequently measured at amortised cost using the effective interest method. The weighted effective interest rate on debt including the effect of derivative financial instruments was 6.63% (30 June 2015: 6.90%).

	DUE DATE	2016 \$M	2015 \$M
Syndicated bank facility A		-	450
Syndicated bank facility B	Apr 2019	415	365
Syndicated bank facility	May 2019	250	250
Euro medium term notes	Apr 2020	485	603
Fixed rate NZD Bonds	May 2021	400	-
Less: facility fees		(10)	(5)
		<b>1,540</b>	<b>1,663</b>
<b>Current</b>		-	-
<b>Non-current</b>		<b>1,540</b>	<b>1,663</b>

#### Syndicated bank facilities

As at 30 June 2016 Chorus had in place \$925 million committed syndicated bank facilities on market standard terms and conditions (30 June 2015: \$1,500 million). The amount of undrawn syndicated bank facilities that is available for future operating activities is \$260 million (30 June 2015: \$435 million).

In April 2016 the maturity of syndicated bank facility B was extended from November 2017 to April 2019. In May 2016 syndicated facility A was repaid and cancelled.

#### Euro Medium Term Notes (EMTN)

FACE VALUE	INTEREST RATE	2016 \$M	2015 \$M
GBP 260 million	6.75%	485	603

Chorus has in place cross currency interest rate swaps to hedge the foreign currency exposure to the EMTN. The cross currency interest rate swaps entitle us to receive GBP principal and GBP fixed coupon payments for NZD principal and NZD floating interest payments. The floating interest rate exposure on the NZD interest payments have been hedged using interest rate swaps.

The syndicated bank facilities are held with bank and institutional counterparties rated -A to AAA, based on rating agency Standard & Poor's ratings.

Chorus utilises hedging instruments to manage the interest rate risk associated with the syndicated bank facilities. Interest rate exposure is managed within Board approved parameters set out in the treasury policy.

The carrying value of syndicated bank facilities approximates their fair value.

The following table reconciles EMTN at hedged rates to EMTN at spot rates as reported under IFRS. EMTN at hedged rates is a non-GAAP measure and is not defined by NZ IFRS.

### Note 3 – Debt (cont.)

	2016 \$M	2015 \$M
EMTN	485	603
Impact of hedged rates used	192	74
<b>EMTN at hedged rates</b>	<b>677</b>	<b>677</b>

The fair value of EMTN, calculated based on the present value of future principal and interest cash flows, discounted at market interest rates at balance date, was \$566 million (30 June 2015: \$690 million)

compared to a carrying value of \$485 million (30 June 2015: \$603 million). This fair value has been determined using Level 2 of the fair value hierarchy as described in note 19.

#### Fixed rate NZD Bonds

	INTEREST RATE	2016 \$M	2015 \$M
Fixed rate NZD Bonds	4.12%	400	-

On 6 May 2016 \$400 million of unsecured, unsubordinated debt securities were issued at a fixed rate of 4.12%. The maturity date is May 2021.

#### Schedule of maturities

	2016 \$M	2015 \$M
Current	-	-
Due 1 to 2 years	-	450
Due 2 to 3 years	665	365
Due 3 to 4 years	485	250
Due 4 to 5 years	400	603
Due over 5 years	-	-
<b>Total due after one year</b>	<b>1,550</b>	<b>1,668</b>
Less: facility fees	(10)	(5)
	<b>1,540</b>	<b>1,663</b>

No debt has been secured against assets. However, there are financial covenants and event of default triggers, as defined in the various debt agreements. During the current year Chorus fully

complied with the requirements set out in its financing agreements (30 June 2015: full compliance).

Refer to note 19 for information on financial risk management.

#### Finance expense

	2016 \$M	2015 \$M
Interest on syndicated bank facility	60	68
Interest on EMTN	53	53
Interest on fixed rate NZD bonds	3	-
Ineffective portion of changes in fair value of cash flow hedges (pre-tax)	9	19
Other interest expense	17	19
Capitalised interest	(5)	(6)
<b>Total finance expense excluding CFH securities</b>	<b>137</b>	<b>153</b>
CFH securities (notional interest)	10	6
<b>Total finance expense</b>	<b>147</b>	<b>159</b>

Other interest expense includes \$13 million finance lease interest expense (30 June 2015: \$13 million), \$1 million of costs relating to the financing of tax payments through Tax Management New Zealand (30 June 2015: \$2 million) and \$3 million

of amortisation arising from the difference between fair value and proceeds realised from the swaps reset (30 June 2015: \$3 million) (refer to note 18).

### Note 3 – Debt (cont.)

The EMTN hedging relationship was reset with a fair value of \$49 million on 9 December 2013 following the close out of the interest rate swaps relating to the EMTN. During the current year ineffectiveness of \$9 million (30 June 2015: \$19 million) flowed through interest expense. A further \$21 million remains in the hedge

reserve and will flow as ineffectiveness to interest expense in the income statement at some time over the life of the derivatives. It will be a non-cash charge. Neither the direction, nor the rate of the impact on the income statement can be predicted.

### Note 4 – CFH securities

Chorus receives funding from the Crown to finance construction costs associated with the development of the UFB network. Chorus receives funding at a rate of \$1,118 for every premises passed (as certified by CFH). In return we issue CFH equity securities, CFH debt securities and CFH warrants. The equity and debt securities have an issue price of \$1 and are issued on a 50:50 basis. For each premises passed, \$559 of equity securities and \$559 of debt securities are issued and we receive \$1,118 funding in return. CFH warrants are issued for nil value. The total committed funding available for Chorus over the period of UFB network construction is expected to be \$929 million.

The CFH equity and debt securities are recognised initially at fair value plus any directly attributable transaction costs. Subsequently they are measured at amortised cost using the effective interest method. The fair value is derived by discounting the \$559 of equity securities and \$559 of debt securities per premises passed by the effective interest rate based on market rates. The difference between funding received (\$1,118 per premises passed) and the fair value of the securities is recognised as Crown funding. Over time, the CFH debt and equity securities increase to face value and the Crown funding is released against depreciation and reduces to nil.

#### CFH equity securities

CFH equity securities are a class of non-interest bearing security that carry no right to vote at meetings of holders of Chorus ordinary shares, but entitle the holder to a preferential right to repayment on liquidation and additional rights that relate to Chorus' performance under its construction contract with CFH.

Dividends will become payable on a portion of the CFH equity securities from 2025 onwards, with the portion of CFH equity securities that attract dividends increasing over time. A greater portion of CFH equity securities attract dividends if the proportion of premises with a fibre connection within Chorus' coverage area at 30 June 2020 does not exceed 20%. The dividend rate will be equal to the New Zealand 180-day bank bill rate plus a margin of 6%. CFH equity instruments can be settled by issuing Chorus shares valued at a 5% discount to the 20-day volume weighted average price for Chorus shares traded in ordinary trading on the NZX Main Board.

The CFH equity securities are treated as a compound financial instrument with a Crown funding component due to the instrument including an interest free loan from a government entity.

On initial recognition, the fair value of the liability component of the compound instrument is calculated using market inputs with no residual amounts allocated to equity. Until the liability component of the compound instrument expires the CFH equity securities are required to be disclosed as a liability. The difference between the face value of the CFH equity securities and the fair value of the liability component is then recorded as Crown funding.

After this, the liability component is measured at amortised cost using the effective interest method and the Crown funding is amortised to depreciation on a systematic basis over the useful lives of the relevant UFB assets.

#### CFH debt securities

CFH debt securities are unsecured, non-interest bearing and carry no voting rights at meetings of holders of Chorus ordinary shares. Chorus is required to redeem the CFH debt securities in tranches from 2025 to 2036 (at the latest) by repaying the face value to CFH. An accelerated repayment schedule applies if the proportion of premises with a fibre connection within Chorus' coverage area at 30 June 2020 does not exceed 20%.

The CFH debt securities are treated as a financial liability with a Crown funding component due to the instrument including an interest free loan from a government entity. On initial recognition the difference between the face value of the CFH debt securities and their fair value (calculated using market inputs) is recorded as Crown funding. After this the liability component is measured at amortised cost using the effective interest method and the Crown funding is amortised to depreciation on a systematic basis over the useful lives of the relevant UFB assets.

The principal amount of CFH debt securities consists of a senior portion and a subordinated portion. The senior portion ranks equally with all other unsecured, unsubordinated creditors of Chorus, and has the benefit of any negative pledge covenant that may be contained in any of Chorus' debt arrangements. The subordinated portion ranks above ordinary shares of Chorus. The initial value of the senior portion is the present value (using a discount rate of 8.5%) of the sum repayable on the CFH debt securities, and the initial subordinated portion will be the difference between the issue price of the CFH debt security and the value of the senior portion.

## Note 4 – CFH securities (cont.)

### CFH warrants

Chorus issues CFH warrants to CFH for nil consideration along with each tranche of CFH equity securities. Each CFH warrant gives CFH the right, on a specified exercise date, to purchase at a set strike price a Chorus share to be issued by Chorus. A CFH warrant will therefore be 'in the money' to the extent that the price that CFH can realise for the Chorus share exceeds the price paid to exercise the CFH warrant. The strike price for a CFH warrant is based on a total shareholder return of 16% per annum on Chorus shares over the period December 2011 to June 2036. Therefore, a holder of a CFH warrant is only likely to exercise the CFH warrant if total shareholder return on Chorus shares has exceeded 16% per annum over the issue date period from June 2025 to June 2036.

At balance date Chorus had issued in total 15,502,118 warrants which had a fair value and carrying value that approximated zero (30 June 2015: 10,987,036 warrants issued). The number of fibre connections made by 30 June 2020 impacts the number of warrants that could be exercised. Should fibre connections at 30 June 2020 exceed 20% then the number of warrants that would be able to be exercised is 6,658,739 (30 June 2015: 4,722,349).

At balance date the component parts of debt and equity instruments including notional interest were:

	2016			2015		
	CFH DEBT SECURITIES \$M	CFH EQUITY SECURITIES \$M	TOTAL CFH SECURITIES \$M	CFH DEBT SECURITIES \$M	CFH EQUITY SECURITIES \$M	TOTAL CFH SECURITIES \$M
<b>Fair value on initial recognition</b>						
Balance as at 1 July	60	37	97	43	26	69
Additional securities recognised at fair value	21	14	35	17	11	28
<b>Balance as at 30 June</b>	<b>81</b>	<b>51</b>	<b>132</b>	<b>60</b>	<b>37</b>	<b>97</b>
<b>Accumulated notional interest</b>						
Balance as at 1 July	6	4	10	3	1	4
Notional interest	5	5	10	3	3	6
<b>Balance as at 30 June</b>	<b>11</b>	<b>9</b>	<b>20</b>	<b>6</b>	<b>4</b>	<b>10</b>
<b>Total CFH securities</b>	<b>92</b>	<b>60</b>	<b>152</b>	<b>66</b>	<b>41</b>	<b>107</b>

The fair value of CFH debt securities at balance date was \$97 million (30 June 2015: \$63 million) compared to a carrying value of \$92 million (30 June 2015: \$66 million). The fair value of CFH equity securities at balance date was \$65 million (30 June 2015: \$41 million) compared to a carrying value of \$60 million (30 June 2015: \$41 million). The fair value has been calculated using discount rates from market rates at balance date and using Level 2 of the fair value hierarchy as described in note 19.

### Key assumptions

Although we believe the estimate of the liability components of the CFH securities on initial recognition is appropriate, the use of different methodologies or assumptions could lead to different measurements of these component parts. The liability components of the CFH securities have been calculated using expected cash flows discounted at risk-adjusted discount rates. As the number of CFH securities expected to be issued increases over time the potential impact of alternative methodologies and assumptions will become increasingly material. Key inputs and assumptions used in these calculations on initial recognition include:

### Discount rate

On initial recognition, the discount rate between 8.46% to 12.05% (30 June 2015: 8.86% to 11.61%) for the CFH equity securities and 5.91% to 8.57% (30 June 2015: 5.98% to 8.14%) for the CFH debt securities used to discount the expected cash flows is based on long dated NZ swap curves. The swap rates were adjusted for Chorus specific credit spreads (based on market observed credit spreads for debt issued with similar credit ratings and tenure). The discount rate on the CFH equity securities is capped at Chorus' estimated cost of (ordinary) equity.

### Expected cash flows

Timing of principal repayments and dividend cash flows has been based on forecasts that reflect economically rational outcomes given the terms of the CFH debt and equity securities.

Repayment dates have been based on an estimate that the proportion of premises with a fibre connection within Chorus' coverage area will exceed 20% at 30 June 2020.

## Note 5 – Crown funding

Funding from the Crown is recognised at fair value where there is reasonable assurance that the funding is receivable and all attached conditions will be complied with. Crown funding is then

recognised in earnings as a reduction to depreciation expense on a systematic basis over the useful life of the asset the funding was used to construct.

	2016				2015			
	UFB \$M	RBI \$M	OTHER \$M	TOTAL \$M	UFB \$M	RBI \$M	OTHER \$M	TOTAL \$M
<b>Fair value on initial recognition</b>								
Balance as at 1 July	304	211	33	548	224	189	28	441
Additional funding recognised at fair value	94	31	6	131	80	22	5	107
<b>Balance as at 30 June</b>	<b>398</b>	<b>242</b>	<b>39</b>	<b>679</b>	<b>304</b>	<b>211</b>	<b>33</b>	<b>548</b>
<b>Accumulated amortisation of funding</b>								
Balance as at 1 July	(10)	(8)	(7)	(25)	(4)	(4)	(5)	(13)
Amortisation	(8)	(6)	(1)	(15)	(6)	(4)	(2)	(12)
<b>Balance as at 30 June</b>	<b>(18)</b>	<b>(14)</b>	<b>(8)</b>	<b>(40)</b>	<b>(10)</b>	<b>(8)</b>	<b>(7)</b>	<b>(25)</b>
<b>Total Crown funding</b>	<b>380</b>	<b>228</b>	<b>31</b>	<b>639</b>	<b>294</b>	<b>203</b>	<b>26</b>	<b>523</b>
<b>Current</b>				<b>17</b>				<b>13</b>
<b>Non-current</b>				<b>622</b>				<b>510</b>

### Ultra-Fast Broadband

Chorus receives funding from the Crown to finance construction costs associated with the development of the UFB network. During the year, Chorus has recognised funding for 121,253 premises passed (30 June 2015: 92,189) where user acceptance testing was complete at 30 June 2016. This brings the total premises passed at 30 June 2016 to approximately 474,000 (30 June 2015: 353,000).

Continued recognition of the full amount of the Crown funding is contingent on certain material performance targets being met. The most significant of these material performance targets relate to the number of premises passed by fibre optic cables by key dates and compliance with certain specifications under user acceptance testing by CFH. Performance targets to date have been met.

## Note 6 – Segmental reporting

An operating segment is a component of an entity that engages in business activities from which it may earn revenues and incur expenses and for which operating results are regularly reviewed by the entity's chief operating decision maker and for which discrete financial information is available.

Chorus' Chief Executive Officer has been identified as the chief operating decision maker for the purpose of segmental reporting.

Chorus has determined that it operates in one segment providing nationwide fixed line access network infrastructure. The determination is based on the reports reviewed by the Chief Executive Officer in assessing performance, allocating resources and making strategic decisions.

All of Chorus' operations are provided in New Zealand, therefore no geographic information is provided.

Three Chorus customers met the reporting threshold of 10% of Chorus' operating revenue in the year to 30 June 2016. The total revenue for the year ending 30 June 2016 from these customers was \$570 million (30 June 2015: \$641 million), \$204 million (30 June 2015: \$164 million) and \$113 million (30 June 2015: \$102 million).

## Note 7 – Operating revenue

Revenue is recognised to the extent that it is probable that the economic benefits will flow to Chorus and the revenue can be reliably measured, regardless of when the payment is being made. Revenue is measured at the fair value of the consideration received or receivable.

Chorus recognises revenue as it provides services to its customers. Billings are generally made on a monthly basis. Unbilled revenues from the billing cycle date to the end of each month are recognised as revenue during the month the service is provided. Revenue is deferred in respect of the portion of fixed monthly charges that have been billed in advance. Revenue from installations and connections is recognised upon completion of the installation or connection.

	2016 \$M	2015 \$M
Basic copper	489	491
Enhanced copper	242	268
Fibre	133	98
Value added network services	35	36
Infrastructure	20	21
Field services	83	84
Other	6	8
<b>Total operating revenue</b>	<b>1,008</b>	<b>1,006</b>

## Note 8 – Operating expenses

	2016 \$M	2015 \$M
Labour costs	78	73
Provisioning	60	58
Network maintenance	89	91
Other network costs	34	34
Information technology costs	65	65
Rent and rates	16	14
Property maintenance	12	11
Electricity	14	14
Insurance	3	4
Consultants	4	3
Regulatory levies	13	15
Other	26	22
<b>Total operating expenses</b>	<b>414</b>	<b>404</b>

### Labour costs

Labour costs of \$78 million (30 June 2015: \$73 million) represents employee costs related to non-capital expenditure.

### Pension contributions

Included in labour costs are payments to the New Zealand Government Superannuation Fund of \$364,000 (30 June 2015: \$357,000) and contributions to KiwiSaver of \$2,980,000 (30 June 2015: \$2,180,000). At 30 June 2016 there were 22 employees in New Zealand Government Superannuation Fund (30 June 2015: 25 employees) and 849 employees in KiwiSaver (30 June 2015: 720 employees). We have no other obligations to provide pension benefits in respect of employees.

### Charitable and political donations

Other costs include charitable donations of \$500 to the Wellington City Mission and \$2,000 to the Equal Employment Opportunities Trust (30 June 2015: \$3,000 to Active Minds Aotearoa). Chorus has not made any political donations (30 June 2015: nil).

### Operating leases

Rent and rates costs include leasing and rental expenditure of \$7 million for property, network infrastructure and items of equipment (30 June 2015: \$5 million).

## Note 8 – Operating expenses (cont.)

### Auditor remuneration

Included in other expenses are fees paid to auditors:

	2016 \$000's	2015 \$000's
Audit and review of statutory financial statements	483	504
Regulatory audit and assurance work <sup>1</sup>	317	397
Tax compliance services	6	3
Other assurance services <sup>2</sup>	4	3
Other services <sup>3</sup>	47	-
<b>Total other services</b>	<b>374</b>	<b>403</b>
<b>Total fees paid to the auditor</b>	<b>857</b>	<b>907</b>

1 Includes the TSO and TDL.

2 Relates to attendance at the Annual Shareholders Meeting (ASM).

3 Other services includes preparation and presentation of hedge accounting training, review of the fibre programme model and sponsorship of an award category at the New Zealand Innovation Awards, run by the New Zealand Innovation Council, which is owned by KPMG.

## Note 9 – Trade and other receivables

Trade and other receivables are initially recognised at the fair value of the amounts to be received, plus transaction costs (if any).

They are subsequently measured at amortised cost (using the effective interest method) less impairment losses.

	2016 \$M	2015 \$M
Trade receivables	126	120
Other receivables	20	35
	<b>146</b>	<b>155</b>
Prepayments	22	21
<b>Trade and other receivables</b>	<b>168</b>	<b>176</b>
<b>Current</b>	<b>158</b>	<b>165</b>
<b>Non-current</b>	<b>10</b>	<b>11</b>

Trade receivables are non-interest bearing and are generally on terms of 20 working days or less.

Chorus maintains a provision for impairment losses when there is objective evidence of its customers being unable to make required payments and makes provision for doubtful debt where debt is more

than 90 days overdue. There have been no significant individual impairment amounts recognised as an expense. Trade receivables are net of allowances for disputed balances with customers.

The ageing profile of trade receivables is as follows:

	2016 \$M	2015 \$M
Not past due	105	106
Past due 1-30 days	18	10
Past due 31-60 days	3	4
Past due 61-90 days	-	-
Past due over 90 days	-	-
	<b>126</b>	<b>120</b>



### Note 9 – Trade and other receivables (cont.)

Chorus has a concentrated customer base consisting predominantly of a small number of retail service providers. The concentrated customer base heightens the risk that a dispute with a customer, or a customer's failure to pay for services, will have a material adverse effect on the collectability of receivables.

Any disputes arising that may affect the relationship between the parties will be raised by relationship managers and follow a dispute resolution process. Chorus has \$21 million of accounts receivable that are past due but not impaired (30 June 2015: \$14 million). The carrying value of trade and other receivables approximate the fair value. The maximum credit exposure is limited to the carrying value of trade and other receivables.

### Note 10 – Trade and other payables

Trade and other payables are initially recognised at fair value less transaction costs (if any). They are subsequently measured at amortised cost using the effective interest method.

	2016 \$M	2015 \$M
Trade payables	98	104
Joint arrangements	-	1
Accruals	176	143
Personnel accrual	19	22
Revenue billed in advance	54	45
<b>Trade and other payables</b>	<b>347</b>	<b>315</b>
<b>Current</b>	<b>347</b>	<b>315</b>
<b>Non-current</b>	<b>-</b>	<b>-</b>

Trade and other payables are non-interest bearing and normally settled within 30 day terms. The carrying value of trade and other payables approximate their fair values.

### Note 11 – Commitments

#### Network infrastructure project agreement

Chorus is committed to deploying infrastructure for premises in the UFB candidate areas awarded to Chorus, to be built according to annual build milestones and to be complete by no later than 31 December 2019. In total it is expected that the communal infrastructure will pass an estimated 830,900 premises. Chorus has estimated that it will cost \$1.75 – \$1.8 billion to build the communal UFB network by the end of 2019.

#### Capital expenditure

Refer to note 1 and note 2 for details of capital expenditure commitments.

#### Lease commitments

Chorus has buildings, car parks and site licenses under operating lease arrangements. The future non-cancellable minimum operating lease commitment as at 30 June 2016 was \$42 million (30 June 2015: \$21 million). Refer to note 14 for further information on leases.

## Note 12 – Taxation

Tax expense comprises current and deferred tax, calculated using the tax rate enacted or substantively enacted at balance date and any adjustments to tax payable in respect of prior years. Tax expense is recognised in the income statement except when it relates to items recognised directly in the statement of comprehensive income, in which case the tax expense is recognised in the statement of comprehensive income.

Deferred tax is recognised in respect of temporary differences between the carrying amounts of assets and liabilities in the financial statements and the amounts used for taxation purposes. A deferred tax asset is recognised only to the extent it is probable it will be utilised.

### Current tax expense

	2016 \$M	2015 \$M
<b>Recognised in income statement</b>		
<b>Net earnings before tax</b>	<b>127</b>	<b>127</b>
Tax at 28%	(36)	(36)
<b>Tax effect of adjustments</b>		
Other non taxable items	–	(1)
Adjustments in respect of prior periods	–	1
<b>Tax expense reported in income statement</b>	<b>(36)</b>	<b>(36)</b>
<b>Comprising:</b>		
Current tax expense	(32)	(28)
Deferred tax expense	(4)	(8)
	<b>(36)</b>	<b>(36)</b>
<b>Recognised in other comprehensive income</b>		
Net movement in cash flow hedge reserve (pre-tax)	32	4
Tax at 28%	9	1
<b>Tax expense reported in other comprehensive income</b>	<b>9</b>	<b>1</b>
<b>Comprising:</b>		
Current tax expense	–	–
Deferred tax expense	9	1
	<b>9</b>	<b>1</b>

### Current tax (receivable)/payable

	2016 \$M	2015 \$M
Balance as at 1 July	12	32
Tax liability for the year	32	28
Tax paid	(47)	(48)
<b>Balance as at 30 June</b>	<b>(3)</b>	<b>12</b>

## Note 12 – Taxation (cont.)

### Deferred tax

(ASSETS)/LIABILITIES	FAIR VALUE PORTION OF DERIVATIVES \$M	EMTN DEBT SECURITIES \$M	CHANGES IN FAIR VALUE OF CASH FLOW HEDGES \$M	NETWORK ASSETS, SOFTWARE AND OTHER INTANGIBLES \$M	FINANCE LEASES \$M	OTHER \$M	TOTAL \$M
Balance at 1 July 2014	(6)	16	1	221	(35)	(5)	192
Recognised in the income statement	–	–	–	6	–	2	8
Recognised in other comprehensive income	–	–	(1)	–	–	–	(1)
<b>Balance as at 30 June 2015</b>	<b>(6)</b>	<b>16</b>	<b>–</b>	<b>227</b>	<b>(35)</b>	<b>(3)</b>	<b>199</b>
Recognised in the income statement	1	(9)	–	11	(2)	3	4
Recognised in other comprehensive income	–	–	(9)	–	–	–	(9)
<b>Balance as at 30 June 2016</b>	<b>(5)</b>	<b>7</b>	<b>(9)</b>	<b>238</b>	<b>(37)</b>	<b>–</b>	<b>194</b>

### Imputation credits

There are \$138 million (30 June 2015: \$120 million) of imputation credits available for subsequent reporting periods. The imputation

credit balance represents the balance of the imputation credit account at the end of the reporting year, adjusted for imputation credits that will arise from the payment of provisional tax relating to the year ended 30 June 2016.

## Note 13 – Cash and call deposits

Cash and call deposits are held with bank and financial institutions counterparties rated at a minimum of A+, based on rating agency Standard & Poor's ratings. Interest earned on call deposits is based on the daily deposit rate.

There are no cash or call deposit balances held that are not available for use.

The carrying values of cash and call deposits approximate their fair values. The maximum credit exposure is limited to the carrying value of cash and call deposits.

Cash and call deposits denominated in foreign currencies are retranslated into New Zealand dollars at the spot rate of exchange at the reporting date. All differences arising on settlement or translation of monetary items are taken to the income statement.

### Cash flow

Cash flows from derivatives in cash flow and fair value hedge relationships are recognised in the cash flow statement in the same category as the hedged item.

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

## Note 14 – Leases

Chorus is a lessee of certain network assets under both operating and finance lease arrangements. Lease costs relating to operating leases are recognised on a straight-line basis over the life of the lease. Finance leases, which effectively transfer substantially all the risks and benefits of ownership of the leased assets, are capitalised at the lower of the leased asset's fair value or the present value of the minimum lease payments at inception of the lease. The leased assets and corresponding liabilities are recognised, and the leased assets are depreciated over their estimated useful lives.

Determining whether a lease agreement is a finance lease or an operating lease requires judgement as to whether the agreement transfers substantially all the risks and rewards of ownership to

Chorus. Judgement is required on various aspects that include, but are not limited to, the fair value of the leased asset, the economic life of the leased asset, whether or not to include renewal options in the lease term, and determining an appropriate discount rate to calculate the present value of the minimum lease payments.

Classification as a finance lease means the asset is recognised in the statement of financial position as network assets whereas for an operating lease no such asset is recognised.

Chorus has exercised its judgement on the appropriate classification of network asset leases, and has determined a number of lease arrangements are finance leases.

### Finance leases

	2016 \$M	2015 \$M
<b>Assets/(liabilities)</b>		
<b>Expected future lease payments:</b>		
Less than one year	(8)	(8)
Between one and five years	(35)	(31)
More than five years	(369)	(372)
<b>Total expected future lease payments</b>	<b>(412)</b>	<b>(411)</b>
Less: future finance charges	280	284
<b>Present value of expected future lease payments</b>	<b>(132)</b>	<b>(127)</b>
<b>Present value of expected future lease payments payable:</b>		
Less than one year	4	3
Between one and five years	15	16
More than five years	(151)	(146)
<b>Total present value of expected future lease payments</b>	<b>(132)</b>	<b>(127)</b>
<b>Classified as:</b>		
Current asset – finance lease receivable	4	3
Non-current liability – finance lease payable	(136)	(130)
<b>Total</b>	<b>(132)</b>	<b>(127)</b>

The carrying value of the finance leases approximates their fair value.

### Property exchanges

Chorus has leased exchange space and commercial co-location space owned by Spark which is subject to finance lease arrangements. Chorus in turn leases exchange space and commercial co-location space to Spark under a finance lease arrangement. The term of the leases vary from three years to ten years and include rights of renewal.

The full term has been used in the calculation of finance lease payables and receivables as it is likely due to the specialised nature of the buildings that the leases will be renewed to the maximum term. The payable and receivable under these finance lease arrangements are net settled in cash. The finance lease arrangement above reflects the net finance lease receivable and payable position.

## Note 14 – Leases (cont.)

### Operating leases

	2016 \$M	2015 \$M
<b>Non-cancellable operating lease rentals are payable as follows:</b>		
Less than one year	6	5
Between one and five years	14	11
More than five years	22	5
<b>Total</b>	<b>42</b>	<b>21</b>

We have entered into leasing arrangements for properties, network infrastructure and other items of equipment which are classified as operating leases. Certain leases are able to be renewed or extended based on terms that would then be agreed with the lessor. There are no other significant lease terms that relate to contingent rents, purchase options or other restrictions on Chorus.

## Note 15 – Equity

### Share capital

Movements in Chorus Limited's issued ordinary shares were as follows:

NUMBER OF SHARES (MILLIONS)	2016 M	2015 M
Balance 1 July	396	396
Dividend reinvestment plan	5	-
<b>Balance at 30 June</b>	<b>401</b>	<b>396</b>

Chorus Limited has 400,799,739 fully paid ordinary shares (30 June 2015: 396,369,767 fully paid ordinary shares). The issued shares have no par value. The holders of ordinary shares are entitled to receive dividends as declared from time to time, and are entitled to one vote per share at meetings of Chorus Limited. Under Chorus Limited's constitution, Crown approval is required if a shareholder wishes to have a holding of 10% or more of Chorus Limited's ordinary shares, or if a shareholder who is not a New Zealand national wishes to have a holding of 49.9% or more of ordinary shares.

On 5 April 2016 a fully imputed interim dividend of 8 cents per share, \$32 million, was paid to shareholders (30 June 2015: no dividends were paid).

The dividend reinvestment plan was resumed for this dividend. Eligible shareholders (those resident in New Zealand or Australia) can choose to have Chorus Limited reinvest all or part of their dividends in additional Chorus Limited shares. For the year ended 30 June 2016, 4,429,972 shares (2015: nil) with a total value of \$17 million (30 June 2015: nil) were issued in lieu of dividends.

Chorus Limited issues securities to CFH based on the number of premises passed. CFH securities are a class of security that carry no right to vote at meetings of holders of Chorus Limited ordinary shares but carry a preference on liquidation. Refer to note 4 for additional information on CFH securities.

Should Chorus Limited return capital to shareholders, any return of capital that arose on demerger is expected to be taxable as Chorus Limited had zero available subscribed capital on demerger.

### Employee share plans

#### Employee equity building scheme

Chorus operates an employee equity building scheme to provide employees the opportunity to become familiar with the shareholder experience. Chorus and eligible employees contribute together to purchase shares on market. The shares are then held by the Trustee (Trustees Executors Limited) and vest to participating employees after a three year period.

A total of 638 employees (30 June 2015: 652 employees) participated in the scheme, 125,290 shares (30 June 2015: 185,168 shares) were purchased at an average price of \$2.67 per share (30 June 2015: \$1.76 per share). At 30 June 2016 the scheme holds 370,259 shares on behalf of 696 employees.

#### Long-term performance share scheme

Chorus operates a long-term performance share scheme (the LTI scheme) for selected key management personnel (participants). The LTI scheme commenced in August 2015 and featured two grants. The shares relating to the first grant have a vesting date of two years from 30 June 2015 (2 year grant), and the shares relating to the second grant have a vesting date of three years from 30 June 2015 (3 year grant). Each grant is made up of two tranches, the first with a relative performance hurdle (Chorus' actual Total Shareholder Return (TSR) compared to other members of the NZX50) and the second with an absolute performance hurdle (Chorus' actual TSR being greater than 10.8% per annum compounding).

## Note 15 – Equity (cont.)

The shares are held by a nominee (Chorus LTI Trustee Limited) on behalf of the participants, until after the shares vest when the nominee is directed to transfer or sell the shares. Or if the shares do not vest they may be held or sold by the nominee. The shares carry the same rights as all other shares.

Participants have been provided with interest-free limited recourse loans to fund the 446,016 shares purchased under the LTI scheme (30 June 2015: nil). The shares were purchased on market at an average price of \$2.69. No shares have been sold or vested during the current period.

The LTI scheme is an equity settled scheme and treated as an option plan for accounting purposes. Each tranche of each grant was valued separately. The tranche with a relative performance hurdle was valued using a Monte Carlo simulation while the tranche with the absolute performance hurdle was valued using the Black Scholes valuation model. The combined option cost for the year ended 30 June 2016 of \$218,000 has been recognised in the income statement (30 June 2015: nil).

Significant assumptions used in the valuation models are:

- a volatility of the Chorus share price in relation to both grants of 36%;
- that dividends will be paid over the term of the scheme; and
- an absolute TSR performance threshold of 10.8%.

## Reserves

### Cash flow hedge reserve

The cash flow hedge reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not yet affected earnings.

For cash flow hedges, the effective portion of gains or losses from remeasuring the fair value of the hedging instrument is recognised in other comprehensive income and accumulated in the cash flow hedge reserve. Accumulated gains or losses are subsequently transferred to the income statement when the hedged item affects the income statement, or when the hedged item is a forecast transaction that is no longer expected to occur. Alternatively, when the hedged item results in a non-financial asset or liability, the accumulated gains and losses are included in the initial measurement of the cost of the asset or liability.

The remeasurement gain or loss on the ineffective portion of a cash flow hedge is recognised immediately in the income statement.

A reconciliation of movements in the cash flow hedge reserve follows:

	2016 \$M	2015 \$M
Opening balance	3	-
Ineffective portion of changes in fair value of cash flow hedges	(7)	(14)
Effective portion of changes in fair value of cash flow hedges	29	16
Amortisation of de-designated cash flow hedges transferred to income statement	1	1
<b>Closing balance</b>	<b>26</b>	<b>3</b>

The periods in which the cash flows associated with cash flow hedges are expected to impact earnings are as follows:

AS AT 30 JUNE 2016	WITHIN 1 YEAR \$M	1-2 YEARS \$M	2-3 YEARS \$M	3-4 YEARS \$M	4-5 YEARS \$M	GREATER THAN 5 YEARS \$M
Cross currency interest rate swaps	-	-	-	(6)	-	-
Interest rate swaps	1	-	7	45	-	-
Forward exchange contracts	3	1	-	-	-	-
Electricity contracts	-	-	-	-	-	-
	<b>4</b>	<b>1</b>	<b>7</b>	<b>39</b>	-	-

AS AT 30 JUNE 2015	WITHIN 1 YEAR \$M	1-2 YEARS \$M	2-3 YEARS \$M	3-4 YEARS \$M	4-5 YEARS \$M	GREATER THAN 5 YEARS \$M
Cross currency interest rate swaps	-	-	-	-	(13)	-
Interest rate swaps	-	1	-	3	32	-
Forward exchange contracts	-	-	-	-	-	-
Electricity contracts	1	-	-	-	-	-
	<b>1</b>	<b>1</b>	-	<b>3</b>	<b>19</b>	-

As at 30 June 2016 the cash flow reserve contained \$25 million of non-cash amounts (30 June 2015: \$21 million) and these have been excluded from the table above.

## Note 15 – Equity (cont.)

### Fair value hedges

Gains or losses from remeasuring the fair value of the hedging instrument are recognised in the income statement together with any changes in the fair value of the hedged asset or liability.

Chorus did not have any hedging arrangements designated as a fair value hedge in the current year (30 June 2015: nil).

## Note 16 – Earnings per share

The calculation of basic earnings per share at 30 June 2016 is based on the net earnings for the year of \$91 million (30 June 2015: \$91 million), and a weighted average number of ordinary shares outstanding during the period of 397 million (30 June 2015: 396 million), calculated as follows:

	2016	2015
<b>Basic earnings per share</b>		
Net earnings attributable to ordinary shareholders (\$ millions)	91	91
Denominator – weighted average number of ordinary shares (millions)	397	396
<b>Basic earnings per share (dollars)</b>	<b>0.23</b>	<b>0.23</b>
<b>Diluted earnings per share</b>		
Net earnings attributable to ordinary shareholders (\$ millions)	91	91
Weighted average number of ordinary shares (millions)	397	396
Ordinary shares required to settle CFH equity securities (millions)	69	68
Ordinary shares required to settle CFH warrants (millions)	7	5
Denominator – diluted weighted average number of shares (millions)	473	469
<b>Diluted earnings per share (dollars)</b>	<b>0.19</b>	<b>0.19</b>

The number of ordinary shares that would have been required to settle all CFH equity securities and CFH warrants on issue at 30 June has been used for the purposes of the diluted earnings per share calculation.

## Note 17 – Related party transactions

### Transactions with related parties

Certain Chorus directors have relevant interests in a number of companies that we have transactions with in the normal course of business. A number of directors are also non-executive directors of other companies. Any transactions undertaken with these entities are in the ordinary course of business.

Chorus has loans to employees and nominees receivable at 30 June 2016 of \$1.2 million (30 June 2015: nil) as outlined in the employee share plan section of note 15. All loans outstanding are interest-free limited recourse loans.

### Key management personnel compensation

	2016 \$000's	2015 \$000's
Short term employee benefits	7,197	6,389
Post employment benefits	–	–
Termination benefits	–	–
Other long term benefits	872	331
Share based payments	218	–
	<b>8,287</b>	<b>6,720</b>

This table above includes remuneration of \$1,012,000 (30 June 2015: \$887,474) paid to directors for the year.

## Note 18 – Derivative financial instruments

Chorus uses derivative financial instruments to reduce its exposure to fluctuations in foreign currency exchange rates, interest rates and the spot price of electricity. The use of hedging instruments is governed by the treasury policy approved by the Board. Derivatives are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured to fair value with an adjustment made for credit risk in accordance with NZ IFRS 13: Fair Value Measurement. The fair values are estimated on the basis of the quoted market prices for similar instruments in an active market or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.

The method of recognising the resulting remeasurement gain or loss depends on whether the derivative is designated as a hedging instrument. If the derivative is not designated as a hedging instrument, the remeasurement gain or loss is recognised immediately in the income statement.

During the year ended 30 June 2014 interest rate swaps with a face value of \$676 million and fair value of \$31 million were reset at the prevailing market interest rates. These transactions realised

\$30 million of cash and resulted in an \$11 million gain being recorded in the cash flow hedge reserve to be amortised over the period to 2020. During the year ended 30 June 2016 amortisation of \$4 million was recognised in finance income (30 June 2015: \$4 million) and \$3 million was recognised in finance expense (30 June 2015: \$3 million). New swaps that hedge the same underlying exposure and risk profile were entered into on the same date, but at a higher effective borrowing cost (4.89% compared to 3.99% prior to the transaction).

Finance expense includes any ineffectiveness arising from the EMTN hedge relationship. Following the close out of the interest rate swaps relating to the EMTN the hedge relationship was reset on 9 December 2013 with a fair value of \$49 million. As long as the hedge remains effective any future gains or losses will be processed through the hedge reserve, however the \$49 million will flow as ineffectiveness to interest expense in the income statement at some time over the life of the derivatives. It will be a non-cash charge. Neither the direction, nor the rate of impact on the income statement can be predicted. For the year ended 30 June 2016 ineffectiveness of \$9 million was recognised in the income statement (30 June 2015: \$19 million).

	2016 \$M	2015 \$M
<b>Current derivative assets</b>		
Cross currency interest rate swaps	1	3
	<b>1</b>	<b>3</b>
<b>Non-current derivative assets</b>		
Cross currency interest rate swaps	–	14
	–	<b>14</b>
<b>Current derivative liabilities</b>		
Interest rate swaps	18	11
Cross currency interest rate swaps	2	–
Forward exchange rate contracts	4	–
Electricity contracts	–	1
	<b>24</b>	<b>12</b>
<b>Non-current derivative liabilities</b>		
Interest rate swaps	57	39
Cross currency interest rate swaps	133	22
Forward exchange rate contracts	1	–
	<b>191</b>	<b>61</b>



## Note 18 – Derivative financial instruments (cont.)

The notional values of contract amounts outstanding are as follows:

	CURRENCY	MATURITY	2016 \$M	2015 \$M
Interest rate swaps	NZD	2016-2020	1,141	1,141
Cross currency interest rate swaps	NZD:GBP	2020	677	677
Forward exchange rate contracts	NZD:AUD	2016	1	–
	NZD:EUR	2016-2017	1	1
	NZD:USD	2016-2018	52	1
	NZD:SEK	2016-2018	19	–
Electricity contracts	NZD	2016-2018	6	8
			<b>1,897</b>	<b>1,828</b>

Credit risk associated with derivative financial instruments is managed by ensuring that transactions are executed with counterparties with high quality credit ratings along with credit

exposure limits for different credit classes. The counterparty credit risk is monitored and reviewed by the Board on a regular basis.

## Note 19 – Financial risk management

### Financial risk management

Chorus' financial instruments consist of cash, short-term deposits, trade and other receivables (excluding prepayments), investments and advances, trade payables and certain other payables, syndicated bank facilities, EMTN, fixed rate NZD bonds, derivative financial instruments and CFH securities. Financial risk management for currency and interest rate risk is carried out by the treasury function under policies approved by the Board. Chorus' risk management policy approved by the Board, provides the basis for overall financial risk management.

Chorus does not hold or issue derivative financial instruments for trading purposes. All contracts have been entered into with major creditworthy financial institutions. The risk associated with these transactions is the cost of replacing these agreements at the current market rates in the event of default by a counterparty.

### Currency risk

Chorus' exposure to foreign currency fluctuations predominantly arise from the foreign currency debt and future commitment to purchase foreign currency denominated assets. The primary objective in managing foreign currency risk is to protect against the risk that Chorus assets, liabilities and financial performance will fluctuate due to changes in foreign currency exchange rates. Chorus enters into foreign exchange contracts, foreign currency options and cross currency interest rate swaps to manage the foreign exchange exposure.

Chorus has issued GBP 260 million foreign currency debt in the form of EMTN. Chorus has in place cross currency interest rate swaps under which Chorus receives GBP 260 million principal and GBP fixed coupon payments for \$677 million principal and floating NZD interest payments. The exchange gain or loss resulting from the translation of EMTN denominated in foreign currency to

New Zealand dollars is recognised in the income statement. The movement is offset by the translation of the principal value of the related cross currency interest rate swap.

As at 30 June 2016, Chorus did not have any significant unhedged exposure to currency risk (30 June 2015: no significant unhedged exposure to currency risk). A 10% increase or decrease in the exchange rate, with all other variables held constant, has minimal impact on profit and equity reserves of Chorus.

### Price risk

In the normal course of business, Chorus is exposed to a variety of financial risks which include the volatility in electricity prices. Chorus has entered into electricity swap contracts to reduce the exposure to electricity spot price movements. Chorus has designated the electricity contracts as cash flow hedge relationships.

A 10% increase or decrease in the spot price of electricity, with all other variables held constant, has minimal impact on profit and equity reserves of Chorus.

### Interest rate risk

Chorus has interest rate risk arising from the cross currency interest rate swap converting the foreign debt into a floating rate New Zealand dollar obligation and the floating rate on the drawn down portion of the syndicated bank facilities. Chorus aims to reduce the uncertainty of changes in interest rates by entering into interest rate swaps to fix the effective interest rate to minimise the cost of net debt and manage the impact of interest rate volatility on earnings. The interest rate risk on the cross currency interest rate swaps has been hedged using interest rate swaps. The interest rate exposure on the syndicated banking facilities has been hedged up to \$465 million with the remaining paying floating interest (30 June 2015: \$215 million).

## Note 19 – Financial risk management (cont.)

### Interest rate repricing analysis

AS AT 30 JUNE 2016	WITHIN 1 YEAR \$M	1-2 YEARS \$M	2-3 YEARS \$M	3-4 YEARS \$M	4-5 YEARS \$M	GREATER THAN 5 YEARS \$M	TOTAL \$M
<b>Floating rate</b>							
Cash and deposits	102	-	-	-	-	-	102
Debt	-	-	200	-	-	-	200
<b>Fixed rate</b>							
Debt (after hedging)	-	-	465	677	400	-	1,542
CFH securities	-	-	-	-	-	152	152
Finance lease (net settled)	(4)	(4)	(5)	(4)	(1)	150	132
	<b>98</b>	<b>(4)</b>	<b>660</b>	<b>673</b>	<b>399</b>	<b>302</b>	<b>2,128</b>

AS AT 30 JUNE 2015	WITHIN 1 YEAR \$M	1-2 YEARS \$M	2-3 YEARS \$M	3-4 YEARS \$M	4-5 YEARS \$M	GREATER THAN 5 YEARS \$M	TOTAL \$M
<b>Floating rate</b>							
Cash and deposits	80	-	-	-	-	-	80
Debt	850	-	-	-	-	-	850
<b>Fixed rate</b>							
Debt (after hedging)	-	215	-	-	677	-	892
CFH securities	-	-	-	-	-	107	107
Finance lease (net settled)	(3)	(4)	(4)	(4)	(4)	146	127
	<b>927</b>	<b>211</b>	<b>(4)</b>	<b>(4)</b>	<b>673</b>	<b>253</b>	<b>2,056</b>

### Sensitivity analysis

A change of 100 basis points in interest rates with all other variables held constant, would increase/(decrease) equity (after hedging) and earnings after tax by the amounts shown below:

	2016 PROFIT OR (LOSS) \$M	2016 EQUITY \$M	2015 PROFIT OR (LOSS) \$M	2015 EQUITY \$M
100 basis point increase	(4)	1	(5)	(6)
100 basis point decrease	4	(2)	5	5

### Credit risk

In the normal course of business, we incur counterparty credit risk from financial instruments, including cash, trade and other receivables, finance lease receivables and derivative financial instruments.

Chorus has certain derivative transactions that are subject to bilateral credit support agreements that require us or the counterparty to post collateral to support the value of certain derivatives. As at 30 June 2016 no collateral was posted.

The maximum exposure to credit risk at the reporting date was as follows:

	NOTES	2016 \$M	2015 \$M
Cash and call deposits	13	102	80
Trade and other receivables	9	146	155
Derivative financial instruments	18	1	17
Finance lease receivable	14	4	3
<b>Maximum exposure to credit risk</b>		<b>253</b>	<b>255</b>

Refer to individual notes for additional information on credit risk.

## Note 19 – Financial risk management (cont.)

### Liquidity risk

Liquidity risk is the risk that we will encounter difficulty raising liquid funds to meet commitments as they fall due or foregoing investment opportunities, resulting in defaults or excessive debt costs. Prudent

liquidity risk management implies maintaining sufficient cash and the ability to meet its financial obligations. Our exposure to liquidity risk based on contractual cash flows relating to financial liabilities is summarised below:

AS AT 30 JUNE 2016	CARRYING AMOUNT \$M	CONTRACTUAL CASH FLOW \$M	LESS THAN 1 YEAR \$M	1-2 YEARS \$M	2-3 YEARS \$M	3-4 YEARS \$M	4-5 YEARS \$M	5+ YEARS \$M
<b>Non derivative financial liabilities</b>								
Trade and other payables	274	274	274	–	–	–	–	–
Finance lease (net settled)	132	412	8	8	7	9	12	368
Debt	1,540	1,841	76	76	739	534	416	–
CFH securities	152	265	–	–	–	–	–	265
<b>Derivative financial liabilities</b>								
Interest rate swaps	75	82	22	22	21	17	–	–
Cross currency interest rate swaps								
Inflows	–	(617)	(33)	(33)	(33)	(518)	–	–
Outflows	135	817	35	34	35	713	–	–
Electricity contracts	–	5	3	2	–	–	–	–
Forward exchange contracts								
Inflows	–	(67)	(50)	(17)	–	–	–	–
Outflows	5	73	54	19	–	–	–	–

AS AT 30 JUNE 2015	CARRYING AMOUNT \$M	CONTRACTUAL CASH FLOW \$M	LESS THAN 1 YEAR \$M	1-2 YEARS \$M	2-3 YEARS \$M	3-4 YEARS \$M	4-5 YEARS \$M	5+ YEARS \$M
<b>Non derivative financial liabilities</b>								
Trade and other payables	248	248	248	–	–	–	–	–
Finance lease (net settled)	127	411	8	8	8	8	8	371
Debt	1,663	1,989	539	75	427	304	644	–
CFH securities	107	200	–	–	–	–	–	200
<b>Derivative financial liabilities</b>								
Interest rate swaps	50	54	14	15	11	8	6	–
Cross currency interest rate swaps								
Inflows	–	(318)	(16)	(16)	(16)	(16)	(254)	–
Outflows	22	375	18	18	18	19	302	–
Electricity contracts	1	6	3	2	1	–	–	–
Forward exchange contracts								
Inflows	–	(2)	(2)	–	–	–	–	–
Outflows	–	2	2	–	–	–	–	–

The gross (inflows)/outflows of derivative financial liabilities disclosed in the previous table represent the contractual undiscounted cash flows relating to derivative financial liabilities held for risk management purposes and which are usually not closed out prior to contractual maturity. The disclosure shows net cash flow amounts for derivatives that are net cash settled and gross cash inflow and outflow amounts for derivatives that have simultaneous gross cash settlement (for example forward exchange contracts).

Chorus manages liquidity risk by ensuring sufficient access to committed facilities, continuous cash flow monitoring and maintaining prudent levels of short term debt maturities.

At balance date, we have available \$260 million under the syndicated bank facilities (30 June 2015: \$435 million).

### Capital risk management

Chorus manages its capital considering shareholders' interests, the value of our assets and credit ratings. The capital Chorus manages consists of cash and debt balances.

The Chorus Board's broader capital management objectives include maintaining an investment grade credit rating with headroom. In the longer term, the Board continues to consider a 'BBB' rating appropriate for a business like ours.

## Note 19 – Financial risk management (cont.)

### Hedge accounting

Chorus designates and documents the relationship between hedging instruments and hedged items, as well as the risk management objective and strategy for undertaking various hedge transactions. At hedge inception (and on an ongoing basis), hedges are assessed to establish if they are effective in offsetting changes in fair values or cash flows of hedged items. Hedge accounting is discontinued if (a) the hedging instrument expires or is sold, terminated, or exercised; (b) the hedge no longer meets the criteria for hedge accounting; or (c) the hedge designation is revoked.

Hedges are classified into two primary types: cash flow hedges and fair value hedges. Refer to note 15 for additional information on cash flow and fair value hedge reserves.

### Fair value

Financial instruments are either carried at amortised cost, less any provision for impairment losses, or fair value. The only significant variances between instruments held at amortised cost and their fair value relates to the EMTN.

For those instruments, recognised at fair value in the statement of financial position, fair values are determined as follows:

Level 1: Quoted market prices – financial instruments with quoted prices for identical instruments in active markets.

Level 2: Valuation techniques using observable inputs – financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.

Level 3: Valuation techniques with significant non-observable inputs – financial instruments valued using models where one or more significant inputs are not observable.

The relevant financial assets and financial liabilities and their respective fair values are outlined in note 18 and are all Level 2 (30 June 2015: Level 2).

### Cross currency interest rate swaps and interest rate swaps

Fair value is estimated by using a valuation model involving discounted future cash flows of the derivative using the applicable forward price curve (for the relevant interest rate and foreign exchange rate) and discount rate.

### Electricity swaps

Fair value is estimated on the ASX forward price curve that relates to the derivative.

The carrying amounts of financial assets and liabilities are as follows:

	CARRIED AT COST OR AMORTISED COST 2016 \$M	CARRIED AT FAIR VALUE 2016 \$M	CARRIED AT COST OR AMORTISED COST 2015 \$M	CARRIED AT FAIR VALUE 2015 \$M
<b>Loans and receivables</b>				
Cash and call deposits	102	–	80	–
Trade receivables	126	–	120	–
Other receivables	20	–	35	–
<b>Designated in a hedging relationship</b>				
Derivative financial assets	–	1	–	17
Derivative financial liabilities	–	(215)	–	(73)
<b>Other financial liabilities</b>				
Trade accounts payable	(98)	–	(104)	–
Joint arrangements	–	–	(1)	–
Accruals	(176)	–	(143)	–
Finance lease (net settled)	(132)	–	(127)	–
Debt	(1,540)	–	(1,663)	–
CFH securities	(152)	–	(107)	–

## Note 20 – Post balance date events

### Dividends

On 29 August 2016 Chorus declared a dividend in respect of year ended 30 June 2016. The total amount of the dividend is \$48.1 million, which represents a fully imputed dividend of 12 cents per ordinary share.

### Commitments

On 8 July 2016 Chorus signed a \$13 million contract with Nokia to upgrade the existing network electronics software for the Copper Provisioning system. Final delivery of the upgrades is September 2017.



# Governance and Disclosures

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## Governance and disclosures

**Chorus' Board and management are committed to ensuring that our people act ethically, with integrity and in accordance with our policies and values.**

### Corporate governance framework

Chorus is incorporated in New Zealand and its shares quoted on the New Zealand and Australian stock exchanges.

Our governance practices and policies reflect, and are consistent with, the:

- NZX Main Board Listing Rules and NZX Corporate Governance Best Practice Code; and
- Financial Markets Authority's Corporate Governance Principles and Guidelines (FMA Corporate Governance Code).

Chorus became an ASX foreign exempt listed issuer in March 2016. Although our governance practices and policies are, as a consequence, no longer required to reflect the ASX listing rules and the ASX Corporate Governance Council's Corporate Governance Principles and Recommendations, we continue to take these into account.

The Board regularly reviews and assesses Chorus' governance policies, processes and practices to identify opportunities for enhancement and to ensure they reflect our operations and culture.

## The Chorus Board

### Role of the Board and delegation of authority

The Board is appointed by Chorus' shareholders and has overall responsibility for Chorus' strategy, culture, health and safety, governance and performance.

The Board's roles and responsibilities are set out in its Charter.

The Board has delegated its authority, in part, to the CEO. The CEO may, in turn, sub-delegate authority to other Chorus people. Formal policies and procedures govern the parameters and operation of these delegations.

The Board has established three standing Board committees to assist it in carrying out its responsibilities. The Board has delegated some of its responsibilities, powers and authorities to those committees. The Board may also establish other ad-hoc Board sub-committees or standing committees and delegate specific responsibilities, powers and authorities to those committees and to particular directors.

The Board and Board committee charters, and other key governance documents, are available on our website at [www.chorus.co.nz/governance](http://www.chorus.co.nz/governance).

### Board membership

The Board seeks to ensure that through its skills mix and composition it is positioned to add value to Chorus.

The Board currently has eight directors (seven independent directors and a managing director) with a broad range of managerial, financial, accounting and industry experience. See pages 10 and 11 for more information on the skills and experience of Chorus' directors.

For a director to be considered independent, the Board must affirmatively determine he or she does not have a disqualifying relationship as set out in the Board Charter.

### Board committees

Board committees assist the Board by focusing on specific responsibilities in greater detail than is possible for the Board as a whole. Each standing Board committee has a Board approved charter and chairman. All standing Board committee members are independent directors.

#### Audit and Risk Management Committee (ARMC)

The ARMC assists the Board in ensuring oversight of all matters relating to Chorus' risk management, financial management and controls and financial accounting, audit and reporting.

Members: Anne Urlwin (chairman), Patrick Strange and Jon Hartley.

#### Human Resources and Compensation Committee (HRCC)

The HRCC assists the Board in overseeing people policies and strategies, including:

- Chorus' remuneration frameworks; and
- Reviewing candidates for, and the performance and remuneration of, the CEO.

Members: Prue Flacks (chairman), Clayton Wakefield, Keith Turner and Murray Jordan.

#### Nominations and Corporate Governance Committee (NCGC)

The NCGC assists the Board in promoting and overseeing continuous improvement of good corporate governance.

The NCGC's role includes:

- Identifying and recommending suitable candidates for nomination as directors and members of Board committees; and
- Establishing, developing and overseeing a process for the Board to annually review and evaluate the performance of the Board, its committees and individual directors.

Members: Patrick Strange (chairman), Jon Hartley and Prue Flacks.

## Board and Board Committee meeting attendance in the year ended 30 June 2016

	REGULAR BOARD MEETINGS	OTHER BOARD MEETINGS <sup>1</sup>	ARMC	HRCC	NCGC	DDC <sup>2</sup>
<b>Total number of meetings held</b>	8	10	4	4	3	5
Patrick Strange	8	10	4		2 <sup>3</sup>	5
Jon Hartley	8	9	3		3	
Anne Urlwin	8	10	4			5
Clayton Wakefield	8	10		4		
Keith Turner	7	8		4	1 <sup>4</sup>	
Mark Ratcliffe	8	10				5
Murray Jordan <sup>5</sup>	7	7		3		
Prue Flacks	8	9		4	2	5

1 Includes dedicated Board health and safety, and strategy and business planning, meetings. In addition, each director also has at least one health and safety site visit each year and Board education sessions are held.

2 A due diligence ad-hoc Board sub-committee was established to oversee Chorus' NZX bond issue.

3 Patrick Strange joined the NCGC on 1 September 2015 and attended all NCGC meetings after that date.

4 Keith Turner was a member of the NCGC until 1 September 2015 and attended the meeting held before that date.

5 Murray Jordan joined the Board and HRCC on 1 September 2015 and attended all regular Board, all HRCC, and 7 out of 8 other Board meetings from that date.

Mark Ratcliffe is not a member of any Board Committees but attends all Board Committee meetings as CEO and as an observer, and may be asked to leave at any time.

### Managing risk

We have a Managing Risk Policy to:

- Ensure the Board sets the risk appetite and reviews principal risks annually;
- Integrate risk management in line with the Board's risk appetite into structures, policies, processes and procedures; and
- Deliver regular principal risk reviews and monitoring.

The Board sets, and annually reviews our risk management framework.

As part of its role, the ARMC is responsible for overseeing and monitoring risk and ensuring compliance with our risk management framework. The ARMC receives regular reporting on risk management, including the management of material business risks and the effectiveness of our internal controls.

### Codes of ethics

We expect our directors and employees to conduct themselves in accordance with the highest ethical standards. We have codes of ethics for our directors and employees that set the expected standards for their professional conduct. These codes are intended to facilitate decisions that are consistent with our values, business goals and legal and policy obligations.

### Trading in Chorus securities

We have an insider trading policy under which:

- Directors must obtain consent from the chairman (or in the chairman's case, the chair of the ARMC) before dealing in Chorus securities; and

- Chorus' "Restricted Persons" must obtain consent from the General Counsel & Company Secretary (or in the General Counsel & Company Secretary's case, the chairman) before dealing in Chorus securities.

Directors and other Chorus people are also prohibited from dealing in Chorus securities while in possession of inside information under the Financial Markets Conduct Act 2013 and the Australian Corporations Act 2001.

### Director induction and education

We have a director induction programme to ensure new directors are appropriately introduced to management and our business.

All directors are expected to continuously educate themselves to ensure they have appropriate expertise to effectively perform their duties. Visits to our operations, briefings from key management, industry experts and key advisers, together with educational and stakeholder visits, briefings and meetings are also arranged for the Board.

### Independent advice

A director may, with the chairman's prior approval (or in the chairman's case the deputy chairman's approval), take independent professional advice (including legal advice) and request the attendance of such advisers at Board and Board committee meetings.

### Review and evaluation of Board performance

The chairman meets with directors to discuss individual performance. The Board has carried out, in the reporting period, a review of the Board's performance, that of individual directors and standing Board committees using the Board evaluation process developed and overseen by the NCGC.

## Market disclosures

We are committed to providing timely, consistent and credible information to promote orderly market behaviour and investor confidence. We believe disclosure should be evenly balanced during good times and bad and that all parties in the investment community have fair access to this information.

## Compliance with corporate governance codes

We consider that during the year ended 30 June 2016:

- The corporate governance principles we adopted and followed did not materially differ from NZX's Corporate Governance Best Practice Code; and
- We met the principles set out in the FMA Corporate Governance Code.

## Corporate Governance Statement

More information on our corporate governance is available in our Corporate Governance Statement available at [www.chorus.co.nz/governance](http://www.chorus.co.nz/governance).

# Diversity at Chorus

## Diversity and inclusiveness at Chorus

We have a Board approved Diversity and Inclusiveness Policy.

We believe that having a team of individuals working together who offer different backgrounds, experiences and perspectives, strengthens our ability to perform as a business.

We define diversity as the characteristics that make one individual similar to, or different from, another and inclusiveness as embracing a variety of people and their views in everyday work, both of which ultimately lead to increased customer and shareholder value.

The focus of our policy is to value differences as a business advantage through attraction and development practices.

We aim to develop our people leaders to behave constructively and in an inclusive way as a core capability, while at the same time recognising and differentiating individual performance.

The HRCC recommends measurable diversity objectives to the Board that are set and assessed annually.

## Diversity metrics as at 30 June 2016

The Board has set the following measurable objectives for achieving greater diversity at Chorus:

MEASURE	DESCRIPTION	AS AT 30 JUNE 2016		AS AT 30 JUNE 2015		BENCHMARK		
Age profiles	Median age	42.2 years		41.7 years		42 years. Statistics New Zealand National Labour Force Projections updated August 2012		
Employee satisfaction	Response to the diversity question "This organisation values differences in education, experience, ideas, work styles and perspectives"	85%		86%		85% Aon Hewitt Best Employer		
Ethnicity by role <sup>1</sup>	Organisational groupings by ethnicity	Total pop'n	People Leaders	Total pop'n	People Leaders	People leader population distribution = total company population distribution		
		Africa	1%	1%	Africa		1%	0%
		Asia	17%	3%	Asia		17%	3%
		Australia	1%	0%	Australia		1%	0%
		Europe	8%	12%	Europe		8%	13%
		Maori	3%	3%	Maori		3%	3%
		New Zealand	64%	79%	New Zealand		63%	79%
		Pacific Island	5%	1%	Pacific Island		5%	1%
South America	0%	1%	South America	0%	1%			
Unknown/not disclosed	1%	0%	Unknown/not disclosed	2%	0%			
Flexible working arrangements	Percentage of the population utilising flexible working arrangements	n/a <sup>2</sup> .		4% working part-time hours		No benchmark determined at this stage		



MEASURE	DESCRIPTION	AS AT 30 JUNE 2016	AS AT 30 JUNE 2015	BENCHMARK																																				
Gender by role	Organisational groupings by gender	<table border="0"> <tr> <td>♀</td> <td>♂</td> <td></td> </tr> <tr> <td>39%</td> <td>61%</td> <td>All</td> </tr> <tr> <td>34%</td> <td>66%</td> <td>People Leaders<sup>3</sup></td> </tr> <tr> <td>22%</td> <td>78%</td> <td>Officers/Senior Executives<sup>4</sup></td> </tr> <tr> <td>29%</td> <td>71%</td> <td>Board<sup>5</sup></td> </tr> <tr> <td>33%</td> <td>67%</td> <td>Non-executive Board<sup>6</sup></td> </tr> </table>	♀	♂		39%	61%	All	34%	66%	People Leaders <sup>3</sup>	22%	78%	Officers/Senior Executives <sup>4</sup>	29%	71%	Board <sup>5</sup>	33%	67%	Non-executive Board <sup>6</sup>	<table border="0"> <tr> <td>♀</td> <td>♂</td> <td></td> </tr> <tr> <td>38%</td> <td>62%</td> <td>All</td> </tr> <tr> <td>34%</td> <td>66%</td> <td>People Leaders<sup>3</sup></td> </tr> <tr> <td>22%</td> <td>78%</td> <td>Officers/Senior Executives<sup>4</sup></td> </tr> <tr> <td>29%</td> <td>71%</td> <td>Board<sup>5</sup></td> </tr> <tr> <td>33%</td> <td>67%</td> <td>Non-executive Board<sup>6</sup></td> </tr> </table>	♀	♂		38%	62%	All	34%	66%	People Leaders <sup>3</sup>	22%	78%	Officers/Senior Executives <sup>4</sup>	29%	71%	Board <sup>5</sup>	33%	67%	Non-executive Board <sup>6</sup>	People leader population distribution = total company population distribution
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Rookie ratio	The previous year's intake by age, ethnicity and gender	Average age 37.3 years Gender 43% ♀ 57% ♂ Africa 2% Asia 19% Australia 7% Europe 15% Maori 1% New Zealand 54% Pacific Island 2% Unknown/not disclosed 0%	Average age 35.9 years Gender 44% ♀ 56% ♂ Africa 2% Asia 25% Australia 1% Europe 10% Maori 1% New Zealand 51% Pacific Island 4% Unknown/not disclosed 6%	No measure – for information																																				
Internal hire rate	The previous year's appointments identifying internal vs external hire rate	47% of all appointments have been internal. 13% of roles in layers 1-3 were appointed from internal candidates <sup>7</sup>	47% of all appointments have been internal. 60% of roles in layers 1-3 were appointed from internal candidates	66% of roles in layers 1-3																																				

- 1 Ethnicity is self-reported.
- 2 A survey was done in 2015 to capture flexible working arrangements as well as part time working. This was a one-off measure collated manually and has not been repeated.
- 3 People Leaders have management and leadership roles within Chorus and other Chorus people formally reporting to them.
- 4 Chorus' Officers/Senior Executives are its CEO and those directly reporting to the CEO other than the Executive Assistant. As at 30 June 2016: Chorus had 2 female and 7 male Officers/Senior Executives (30 June 2015: 2 female, 7 male).
- 5 As at 30 June 2016: Chorus had 2 female and 6 male directors (30 June 2015: 2 female, 5 male).
- 6 As at 30 June 2016: Chorus had 2 female and 5 male non-executive directors (30 June 2015: 2 female, 4 male).
- 7 Layers 1-3 means the CEO, those reporting to the CEO, and those reporting to them. Eight total hires were made at layers 1-3, one was an internal appointment.

Based on the annual review of effectiveness of Chorus' Diversity and Inclusiveness Policy and our measurable diversity objectives, the Board considers that overall we are making good progress towards achieving our diversity and inclusiveness objectives and have performed well against the policy generally. We do not yet have the balance of diversity we aspire to in all areas and are focused on improving. We have carried out an independent diversity and inclusiveness review and established a Diversity Council and diversity and inclusiveness Executive Steering Group. These set a platform for leveraging further diversity and inclusiveness initiatives into our highly engaged team.

The chairman and CEO are part of the Champions for Change initiative in New Zealand.

## Remuneration and performance

### Remuneration model

Our remuneration model is designed to align employee and shareholder interests and to be simple, clear and fair. It aims to attract, retain and motivate high-calibre employees to all levels of the Company, at the same time driving performance, customer focus and personal development. The Board regularly reviews our remuneration design.

All employees have fixed remuneration, targeted at the market median and the potential to earn a Short Term Incentive (STI). The CEO and members of the executive leadership team have the potential to earn a Long Term Incentive (LTI). Both STI and

LTI are variable elements of remuneration and are only paid if both Company and individual performance goals have been met.

We have expanded our disclosure this year, including CEO remuneration.

### Fixed remuneration

Fixed remuneration is adjusted each year based on data from independent remuneration specialists. Employees' fixed remuneration is based on a matrix of their own performance and their current position when compared to the market.

### Short term incentive

STI values are set as a percentage of fixed remuneration, from 5% to 33% based on the complexity of the role. The CEO has an STI as a percentage of fixed remuneration as set out later in this report. STI payments are determined following a review of Company and individual performance and paid out at a multiplier of between 0x and 1.75x for the CEO and executive leadership team, and between 0x and 2.8x for all other employees. (Prior to the year ended 30 June 2016, the CEO and executive leadership team values were also 0x and 2.8x). This model is based on clear goals, differentiating performance and rewarding delivery.

Company performance goals are set and reviewed annually by the Board to align with shareholder value. If Company goals are not met, including a preliminary "gateway" goal, no STI is payable. In the year ended 30 June 2016, the Company goals were:

- 50% based on EBITDA performance against budget;
- 30% based on achieving fibre connection capex budgets and service level performance targets; and
- 20% based on achieving certain strategic initiatives.

Individual performance goals for all employees are tailored to their role, with 70% of the goals based on 'what' they achieve and 30% based on 'how' they perform their role, which includes a health and safety component for all people leaders.

As an example of how STI is calculated, an employee with fixed remuneration of \$80,000 and an STI element of 10% may receive between \$0 and \$22,400 (0x to 2.8x their STI percentage) depending on the level of Company performance and their individual performance.

### CEO remuneration for performance periods ending 30 June 2016 and 30 June 2015

	FIXED REMUNERATION			PAY FOR PERFORMANCE				TOTAL REMUNERATION
	SALARY	NON-TAXABLE BENEFITS <sup>1</sup>	SUBTOTAL	STI	STI EXTENSION <sup>4</sup>	LTI	SUBTOTAL	
FY16	895,868	20,800	916,668	772,200 <sup>2</sup>	371,029	189,379 <sup>5</sup>	1,332,608	2,249,276
FY15	831,355	20,800	852,155	739,908 <sup>3</sup>	185,515	99,565 <sup>6</sup>	1,024,988	1,877,143

### Five Year Remuneration Summary

	TOTAL REMUNERATION	% STI AWARDED AGAINST MAXIMUM	% LTI AWARDED AGAINST MAXIMUM	% STI EXTENSION AWARDED AGAINST MAXIMUM	SPAN OF LTI PERFORMANCE PERIOD
FY16	2,249,276	75%	70%	100%	FY13 – FY15
FY15	1,877,143	57%	69%	100%	FY12 – FY14
FY14	1,696,507	40%	107%	-	FY11 – FY13
FY13	1,227,419	34%	-	-	-
FY12 <sup>7</sup>	1,094,351	56%	-	-	-

1 Accommodation allowance in place of hotel/meal costs in Auckland (CEO Wellington based).

2 STI for FY16 performance period (paid FY17)

3 STI for FY15 performance period (paid FY16)

4 STI Extension for performance period FY14 to FY16 in place of LTI (scheme has now ended)

5 LTI for performance period FY13 to FY15 (vested FY16)

6 LTI for performance period FY12 to FY14 (vested FY15)

7 Seven months ended 30 June 2012

Other benefits

Company KiwiSaver contributions: FY16: \$65,806 (FY15: \$49,055)

Medical insurance: FY16: \$7,064 (FY15: \$6,877)

### Short term incentive extension programme

This was a temporary programme put in place in December 2013 based on specific performance criteria to reward and retain key executives through a period of change and uncertainty. For the CEO the value was a maximum of 66.6% of base salary across a two year period, with payment weighted  $\frac{1}{3}$  for the first year and  $\frac{2}{3}$  for the second year. The scheme has now ended.

### Long term incentives

We offer long term incentives to incentivise and retain key executives, align the interests of executives and shareholders and encourage longer term decision making. In August 2015, a new LTI share scheme was established to apply for the first time in the year ended 30 June 2016 (described in more detail in Note 15 of the financial statements). This replaced the previous LTI and STI Extension programmes which were established following demerger.

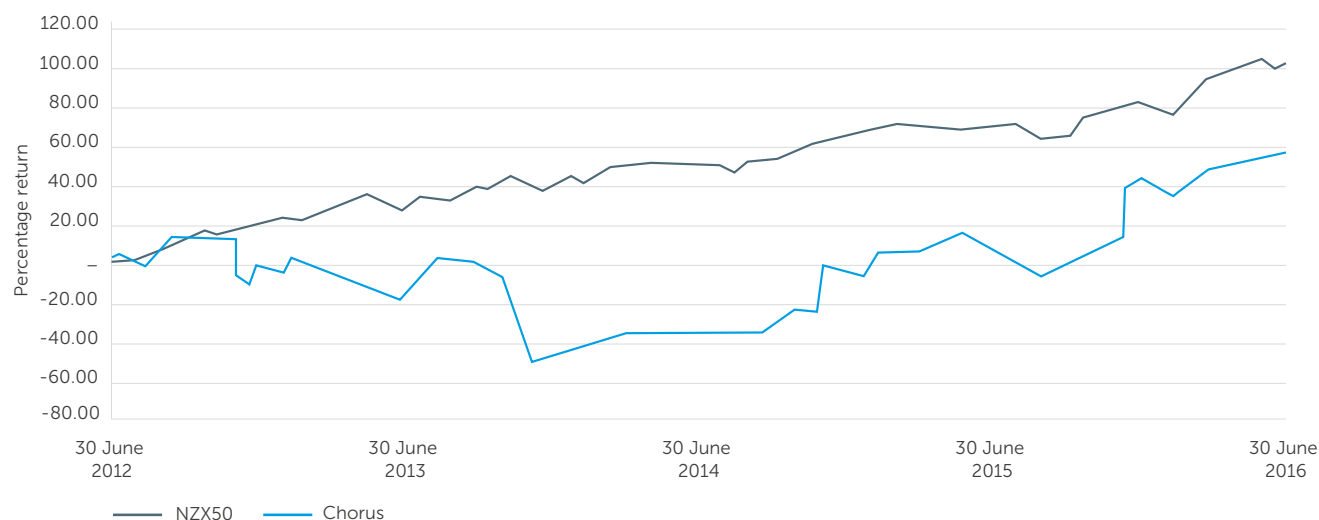
### Employee equity building scheme

We implemented an employee equity building scheme in 2013 to encourage employees to think and act as shareholders of the Company. The Shares under the scheme are held by a trustee and vest to eligible employees after a three year period. For more details, refer to Note 15 of the financial statements.

### CEO remuneration

The CEO's remuneration consists of fixed remuneration, an STI and an LTI. This is reviewed annually by the HRCC and Board after reviewing Chorus' performance, the CEO's individual performance and advice from external remuneration specialists.

Five Year Summary – Total Shareholder Return (TSR) Performance



The TSR summary above shows the performance of Chorus' shares against the NZX50 between 30 June 2012 and 30 June 2016.

Description of CEO STI, STI extension and LTI schemes for performance period ending 30 June 2016

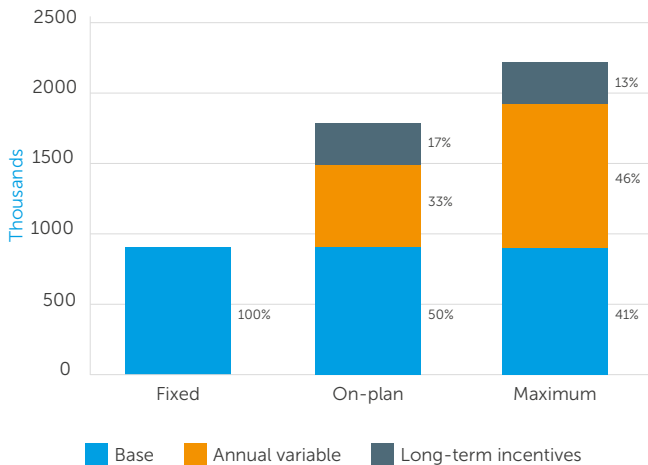
SCHEME	DESCRIPTION	PERFORMANCE MEASURES	PERCENTAGE OF MAXIMUM AWARDED
STI	Set at 65% of base remuneration for FY16 on-plan performance, up to a maximum of 1.75x or 114% of base remuneration where the highest levels of both company and individual performance measures are achieved.	<p>Company performance measures:</p> <ul style="list-style-type: none"> <li>50% on EBITDA performance against operating plan.</li> <li>30% on fibre connection capex and service level performance targets.</li> <li>20% on strategic initiatives.</li> </ul> <p>Individual performance measures:</p> <ul style="list-style-type: none"> <li>25% on operating plan goals.</li> <li>20% on Chorus reputation.</li> <li>25% on management of regulatory issues.</li> <li>30% on fibre connections and customer experience.</li> </ul>	75% \$772,200 Paid in August 2016.
STI extension	A temporary scheme put in place in December 2013 in place of a LTI to incentivise and retain key executives through a period of change and uncertainty. A maximum of 66.6% of base salary for the performance period FY14 to FY16, with payment weighted 1/3 in FY15 and 2/3 in FY16. The scheme has now ended.	<ul style="list-style-type: none"> <li>CEO employed by Chorus at time of payment.</li> <li>STI company performance measures for prior year achieved.</li> <li>Mid-year results on track to operating plan for current year.</li> </ul>	100% \$371,029 Vested March 2016.
LTI	Cash grant of \$349,779 (gross) for performance period FY13-FY15 (3 years). This converted to Equity Equivalent Units (EEU's) by dividing the target value by the volume weighted average price of Chorus shares for a defined 20 day trading period. This equated to a maximum of 104,853 EEU's. These were converted back to a cash value, based on share price performance at the time of vesting in FY16.	<ul style="list-style-type: none"> <li>90% on achieving UFB programme targets including build and connection measures.</li> <li>10% on achieving a range of RBI programme targets.</li> </ul>	70% \$189,379 Vested September 2015.

Grants made under the LTI scheme to the CEO in the year ending 30 June 2016

SCHEME	DESCRIPTION	MEASURES	VESTING
Shares	Two-year grant made 1 July 2015, equivalent to 33% of base remuneration on entry (\$278,272), divided into two tranches of \$139,136 each.	Tranche 1: Relative TSR performance against NZX50 (fixed at date of grant) with 50% vesting at 50th percentile and 100% vesting at 75th percentile (pro-rata in between).  Tranche 2: TSR performance over vesting period must exceed 10.8% on an annualised basis, compounding.	Due to vest in FY18
Shares	Three-year grant made 1 July 2015, equivalent to 33% of base remuneration on entry (\$278,272), divided into two tranches of \$139,136 each.	Tranche 1: Relative TSR performance against NZX50 (fixed at date of grant) with 50% vesting at 50th percentile and 100% vesting at 75th percentile (pro-rata in between).  Tranche 2: TSR performance over vesting period must exceed 10.8% on an annualised basis, compounding.	Due to vest in FY19

CEO remuneration performance pay

The scenario chart below demonstrates the elements of CEO remuneration design in the year ended 30 June 2016. For on-plan performance, the STI element pays out at 65% of base salary and the LTI element pays out at 33% of base salary. At maximum performance, the STI element pays out at 114% of base salary, the LTI element remains at 33%.



## Employee remuneration range during the year ended 30 June 2016

The table below shows the number of employees and former employees who received remuneration and other benefits in excess of \$100,000 during the year ended 30 June 2016.

During the year, certain employees participated in Chorus' employee equity building scheme, received contributions towards membership of the Marram Trust (a community healthcare and holiday accommodation provider), received contributions toward their Government Superannuation Fund (a legacy benefit provided to a small number of employees) and, if a member, received contributions of 3% of gross earnings towards their KiwiSaver accounts. These amounts are not included in these remuneration figures. Any benefits received by employees that do not have an attributable value are also excluded.

The remuneration paid to, and other benefits received by, Mark Ratcliffe in his capacity as CEO during the year ended 30 June 2016 are detailed on pages 64 to 66, and are excluded from the table below.

REMUNERATION RANGE \$ (GROSS)	NUMBER OF EMPLOYEES IN THE YEAR ENDED 30 JUNE 2016 (BASED ON ACTUAL PAYMENTS)
950,001-960,000	1
660,001-670,000	2
610,001-620,001	1
590,001-600,000	1
520,001-530,000	1
410,001-420,000	1
380,001-390,000	1
350,001-360,000	1
330,001-340,000	1
320,001-330,000	2
300,001-310,000	2
280,001-290,000	3
270,001-280,000	2
260,001-270,000	3
250,001-260,000	4
240,001-250,000	6
230,001-240,000	5
220,001-230,000	11
210,001-220,000	11
200,001-210,000	5
190,001-200,000	15
180,001-190,000	14
170,001-180,000	15
160,001-170,000	22
150,001-160,000	30
140,001-150,000	40
130,001-140,000	39
120,001-130,000	45
110,001-120,000	47
100,000-110,000	53

## Pay gap

The pay gap represents the number of times greater the CEO remuneration is to an employee paid at the median of all Chorus employees. At 30 June 2016, the CEO's base salary at \$895,868 was 10.33 times that of the median employee at \$86,700 per annum. The CEO's total remuneration, including STI, STI extension and LTI was \$2,249,276 which was 22.43 times the total remuneration of the median employee (including STI) at \$100,272.

## Director remuneration

The Board has adopted the fee structure below. The Board appointed a deputy chairman from 1 September 2015 with a fee reflecting the additional work that role entails. Total remuneration available to non-executive directors in the year ended 30 June 2016 was fixed at our 2014 annual shareholders' meeting at \$1,100,000.

The HRCC reviews the remuneration of directors annually based on criteria developed by that Committee.

ANNUAL FEE STRUCTURE	YEAR ENDED 30 JUNE 2016 \$
<b>Base fees:</b>	
Chairman of the Board	214,000
Deputy chairman	160,500
Non-executive director	107,000
<b>Board Committee fees:</b>	
<b>Audit and Risk Management Committee</b>	
Chairman	32,000
Member	16,000
<b>Human Resources and Compensation Committee</b>	
Chairman	21,500
Member	11,000
<b>Nominations and Corporate Governance Committee</b>	
Chairman	16,000
Member	8,500
<b>UFB Steering Committee</b>	
Member	32,000

Standing Board committee and UFB Steering Committee fees are paid to directors, except the chairman and deputy chairman of the Board, in addition to base fees. Directors (except the CEO) do not participate in a bonus or profit-sharing plan, do not receive compensation in share options, and do not have superannuation or any other scheme entitlements or retirement benefits.

Directors may be paid an additional daily rate of \$2,400 for additional work as determined and approved by the chairman and where the payment is within the total fee pool available. No such fees were paid in the year ended 30 June 2016.

Remuneration paid to directors (in their capacity as such) in the year ended 30 June 2016:

DIRECTOR	TOTAL FEES \$
Patrick Strange (chairman) <sup>1</sup>	198,833
Jon Hartley (deputy chairman) <sup>2</sup>	169,417
Anne Urlwin	139,000
Clayton Wakefield	124,578
Keith Turner	151,417
Mark Ratcliffe	-
Murray Jordan <sup>3</sup>	98,333
Prue Flacks	130,422
<b>Total</b>	<b>1,012,000</b>

1 Patrick Strange became chairman on 1 September 2015.

2 Jon Hartley was interim chairman until 1 September 2015, and became deputy chairman from that date.

3 Murray Jordan joined the Chorus Board on 1 September 2015.

**Notes:**

Amounts are gross and exclude GST (where applicable).

Mark Ratcliffe, as CEO, does not receive any remuneration in his capacity as a director.

Directors (other than the CEO) did not receive any other benefits.

In addition Directors are entitled to be reimbursed for any travel or incidental expenses incurred in performance of their duties as director.

## Disclosures

### Directors

#### Directors during the year ended 30 June 2016

No directors resigned during the year ended 30 June 2016.

Patrick Strange was appointed chairman and Jon Hartley deputy chairman on 1 September 2015. Murray Jordan was appointed director also on 1 September 2015.

#### Indemnities and insurance

We have entered into deeds of indemnity with each director for potential liabilities or costs they may incur for their acts or omissions as directors.

#### Director interests in Chorus shares

As at 30 June 2016, directors had a relevant interest (as defined in the Financial Markets Conduct Act 2013) in approximately 0.086% of Chorus' shares as follows:

DIRECTOR	AS AT 30 JUNE 2016		TRANSACTIONS DURING THE REPORTING PERIOD			
	SHARES	INTEREST	NUMBER OF SHARES	NATURE OF TRANSACTION	CONSIDERATION	DATE
Patrick Strange	10,000	Beneficial interest	10,000	On-market acquisition	\$25,700.00	25 August 2015
Anne Urlwin	10,192	Director and shareholder of registered holder	192	Acquisition under Chorus' dividend reinvestment plan	\$742.75	5 April 2016
Clayton Wakefield <sup>1</sup>	21,110	Beneficial interest	398	Acquisition under Chorus' dividend reinvestment plan	\$1,539.66	5 April 2016
Keith Turner	6,109	Legal and beneficial interest	115	Acquisition under Chorus' dividend reinvestment plan	\$444.88	5 April 2016
Mark Ratcliffe	147,967	Beneficial interest	2,794	Acquisition under Chorus' dividend reinvestment plan	\$10,808.59	5 April 2016
			145,173	Off-market transfers to family trust	Nil	16 December 2015
			39,840	On-market acquisition	\$99,161.90	7 September 2015
	138,654	Beneficial interest (under Chorus' long term incentive plan)	138,654 <sup>2</sup>	On-market purchase of shares granted under Chorus' long term incentive plan	\$372,882.20	29 September – 1 October 2015
Prue Flacks	10,582	Registered holder and beneficial owner	200	Acquisition under Chorus' dividend reinvestment plan	\$773.70	5 April 2016
			5,240	Off-market transfer on distribution of estate and family trust	Nil	4 February 2016
<b>Total</b>	<b>344,614</b>					

1 Clayton Wakefield also acquired a beneficial interest in 76,000 Chorus bonds quoted on the NZX on their issue on 6 May 2016.

2 Shares held by trustee and vest subject to certain performance targets being met over the periods ending 30 June 2017 and 30 June 2018.

## Changes in director interests

Patrick Strange	Became a director of Auckland International Airport Limited and New Zealand Clearing and Depository Corporation Limited (a subsidiary of NZX Limited).  Ceased as director of WorkSafe New Zealand.
Jon Hartley	Ceased as a trustee of Yorkshire Trust.
Clayton Wakefield <sup>1</sup>	Became Chairman of the Auckland Branch, and a National Council Member, of the Institute of Directors.  Ceased as a director of Equipment Finance Limited.
Keith Turner	Became a director of TransGrid (the operator and manager of the New South Wales high voltage transmission network).
Mark Ratcliffe	Became a director of The New Zealand Initiative Limited; Gas Services NZ Limited; First Gas Topco Limited (and its subsidiaries First Gas Holdings Limited, First Gas Limited, First Gas Midco Limited).
Murray Jordan <sup>2</sup>	Became a trustee of The Starship Foundation and a director of Metcash Limited and Real Clarity Limited.

1 Became a director of The Co-operative Bank Limited on 25 August 2016 and ceased as a director of: Fisher & Paykel Finance Limited; Fisher & Paykel Finance Holdings Limited; Fisher & Paykel Financial Services Limited; Consumer Finance Limited; Consumer Insurance Services Limited; Columbus Financial Services Limited and Retail Financial Services Limited on 17 July 2016.

2 Became a director of Stevenson Group Limited on 14 July 2016.

## Director restrictions

Under our constitution, no person who is an 'associated person' of a telecommunications services provider in New Zealand may be appointed or hold office as a director. NZX has granted Chorus a waiver to allow our constitution to include this restriction.

## External audit

The non-audit related fees paid to the auditor during the financial period (as detailed in Note 8 to the Financial Statements) were permitted non-audit services under our External Auditor Independence Policy.

## Securities and security holders

### Stock exchange listings and American Depositary Receipts

Chorus' shares are quoted on the NZX Main Board and on the ASX. Chorus changed to an ASX foreign exempt listing on the ASX on 1 March 2016.

Chorus trades under the ticker 'CNU'.

American Depositary Shares, each representing five ordinary shares and evidenced by American Depositary Receipts, are not listed but are traded on the over-the-counter market in the United States under the ticker 'CHRY'. Our depository is the Bank of New York Mellon.

We issued NZD400 million of bonds on 6 May 2016 which are quoted on the NZX debt market (the NZDX).

We have also issued GBP260 million foreign currency debt in the form of European medium term notes (EMTNs). Chorus is listed, and the EMTNs quoted, on the Luxembourg Stock Exchange.

### NZX waivers

A summary of all waivers granted and published by NZX in the 12 months ending on 30 June 2016 and relied on by Chorus is available on Chorus' website at [www.chorus.co.nz/investor-centre](http://www.chorus.co.nz/investor-centre).

### ASX disclosures

- Chorus' place of incorporation is New Zealand.
- Chorus is not subject to Chapters 6, 6A, 6B and 6C of the Australian Corporations Act 2001 dealing with the acquisition of shares (including substantial shareholdings and takeovers).
- Chorus' constitution contains limitations on the acquisition of securities, as described below.
- For the purposes of ASX listing rule 1.15.3 Chorus confirms that it continues to comply with the NZX listing rules.

### Registration as a foreign company

Chorus has registered with the Australian Securities and Investments Commission as a foreign company. Chorus has been issued an Australian Registered Body Number (ARBN) of 152 485 848.

### Quoted shares

As at 30 June 2016 there were 400,799,739 ordinary shares on issue.

Each ordinary share confers on its holder the right to attend and vote at a shareholder meeting (including the right to cast one vote on a poll on any resolution).

### Non-standard designation

NZX has attached a 'non-standard' designation to Chorus because of the ownership restrictions in our constitution (described below).

### Chorus' constitutional ownership restrictions

Our constitution includes ownership restrictions that prohibit any person:

- From having a relevant interest in 10% or more of Chorus' shares, unless the prior written consent of the New Zealand Government is obtained; or
- Other than a New Zealand national, from having a relevant interest in more than 49.9% of Chorus' shares, unless the prior written consent of the New Zealand Government is obtained.



If the Board or the New Zealand Government determines there are reasonable grounds for believing that a person has a relevant interest in voting shares in excess of the ownership restrictions, the Board may, after following certain procedures, prohibit the exercise of voting rights (in which case the voting rights shall vest in the chairman) and may force the sale of shares. The Board may also decline to register a transfer of shares if it reasonably believes the transfer would breach the ownership restrictions.

NZX has granted Chorus waivers allowing our constitution to include the power of forfeiture, the restrictions on transferability of Chorus shares and the Board's power to prohibit the exercise of voting rights relating to these ownership restrictions.

We have been advised by the Crown that AMP Capital Holdings Ltd and its related companies have been granted approval, should they choose to exercise it in future, to acquire a relevant interest in 10% or more (but not exceeding 15%) of Chorus shares.

#### Unquoted securities

SECURITY	NUMBER OF SECURITIES ISSUED IN YEAR ENDED 30 JUNE 2016	TOTAL NUMBER OF SECURITIES ON ISSUE AS AT 29 JULY 2016	HOLDER	PERCENTAGE HELD
CFH Equity Securities	71,380,402	265,204,693	Crown Fibre Holdings Ltd	100%
CFH Debt Securities	71,380,402	265,204,693	Crown Fibre Holdings Ltd	100%
CFH Warrants	4,515,082	15,502,118	Crown Fibre Holdings Ltd	100%

CFH equity securities are a unique class of security that carry no right to vote at meetings of holders of ordinary shares but entitle the holder to a right to a repayment preference on liquidation. Dividends become payable on a portion of CFH equity securities from 2025, with the portion increasing over time. A greater portion of CFH equity securities attract dividends if a 20% fibre up-take threshold is not met by 30 June 2020. CFH equity securities can be redeemed by Chorus at any time by payment of the issue price or issue of new ordinary shares (at a 5% discount to the 20-day volume weighted average price) to the holder. In limited circumstances CFH equity securities may be converted by the holder into voting preference or ordinary shares.

CFH debt securities are unsecured, non-interest bearing and carry no voting rights at meetings of holders of ordinary shares. Chorus is required to redeem the CFH debt securities in tranches from 2025 to 2036 (at the latest) by repaying the issue price to the holder. An accelerated repayment schedule applies if a 20% fibre up-take threshold is not met by 30 June 2020. CFH warrants are an option to acquire ordinary shares on a specified exercise date at a set strike price and have been issued in two series, with different repayment schedules. On 30 June 2020 one series will be cancelled depending on whether a 20% fibre up-take threshold is met.

The terms of issue for the CFH equity securities, CFH debt securities and CFH warrants are set out in the subscription agreement with CFH and summarised on Chorus' website at [www.chorus.co.nz/financial-results](http://www.chorus.co.nz/financial-results).

#### Shareholder distribution as at 29 July 2016

SHAREHOLDING	NUMBER OF HOLDERS	% OF TOTAL HOLDERS	TOTAL NUMBER OF SHARES HELD	% OF ORDINARY SHARES ISSUED
1 to 1,000	16,213	64.20%	5,918,274	1.48%
1,001 to 5,000	6,029	23.88%	14,851,815	3.71%
5,001 to 10,000	1,647	6.52%	11,978,481	2.99%
10,001 to 100,000	1,281	5.07%	29,098,663	7.26%
100,001 and over	82	0.32%	338,952,506	84.57%
<b>Total</b>	<b>25,252</b>	<b>100%</b>	<b>400,799,739</b>	<b>100%</b>

#### Substantial holders

We have received notice of substantial product/security holders as follows:

	AS AT 30 JUNE 2016	AS AT 29 JULY 2016
	NUMBER ORDINARY SHARES HELD	NUMBER ORDINARY SHARES HELD
Paradise Investment Management Pty Ltd	20,282,796	20,282,796
Accident Compensation Corporation	28,293,763	28,293,763

### Twenty largest shareholders as at 29 July 2016

RANK	HOLDER NAME	HOLDING	%
1.	New Zealand Central Securities Depository Limited*	143,596,777	35.82
2.	JP Morgan Nominees Australia Limited	46,758,832	11.66
3.	National Nominees Limited	32,266,133	8.05
4.	Citicorp Nominees Pty Limited	22,678,364	5.65
5.	HSBC Custody Nominees (Australia) Limited	21,189,535	5.28
6.	RBC Investor Services Australia Nominees Pty Limited <Bkcust A/C>	12,159,939	3.03
7.	FNZ Custodians Limited	7,443,787	1.85
8.	Ronald James Woodrow	5,075,834	1.26
9.	HSBC Custody Nominees (Australia) Limited <NT-Comnwlth Super Corp A/C>	4,897,169	1.22
10.	Bond Street Custodians Limited <Macq High Conv Fund A/C>	4,061,597	1.01
11.	HSBC Custody Nominees (Australia) Limited <A/C 3>	3,201,745	0.79
12.	Citicorp Nominees Pty Limited <Colonial First State Inv A/C>	2,237,012	0.55
13.	Custodial Services Limited <A/C 3>	2,133,807	0.53
14.	BNP Paribas Noms Pty Ltd <Drp>	1,975,843	0.49
15.	New Zealand Depository Nominee Limited < A/C 1> Cash Account	1,959,785	0.48
16.	Investment Custodial Services Limited <A/C C>	1,736,987	0.43
17.	Forsyth Barr Custodians Limited <1-Custody>	1,685,901	0.42
18.	NZPT Custodians (Grosvenor) Limited	1,668,519	0.41
19.	Bond Street Custodians Limited <Macquarie Smaller Co's A/C>	1,144,704	0.28
20.	Custodial Services Limited <A/C 2>	1,126,914	0.28

\* New Zealand Central Securities Depository Ltd provides a custodial depository service which allows electronic trading of securities by its members.

### Net tangible assets per security

As at 30 June 2016, consolidated net tangible assets per share was \$1.77 (30 June 2015: \$1.62). Net tangible assets per share is a non-GAAP financial measure and is not prepared in accordance with NZIFRS.

### Revenue from ordinary activities and net profit

In the year ended 30 June 2016 our:

- Revenue from ordinary activities increased 0.2% to \$1,008 million; and
- Profit from ordinary activities after tax, and net profit, attributable to shareholders did not change at \$91 million.

### Subsidiaries

#### Chorus New Zealand Ltd

Directors: Mark Ratcliffe (chairman), Andrew Carroll, Nick Woodward, Vanessa Oakley and Lucy Riddiford (as alternate director for Vanessa Oakley).

No Chorus New Zealand Ltd directors resigned in the year ended 30 June 2016.

#### Director remuneration

The directors of Chorus New Zealand Ltd are all employees and do not receive any remuneration in their capacity as directors.

#### Changes in director interests

Mark Ratcliffe: Acquired a beneficial interest in 138,654 Chorus Ltd shares under Chorus' Long Term Incentive plan and became a director of The New Zealand Initiative Limited; Gas Services NZ Limited; First Gas Topco Limited (and its subsidiaries First Gas Holdings Limited, First Gas Limited, First Gas Midco Limited).

#### Chorus LTI Trustee Ltd

Chorus LTI Trustee Ltd was incorporated on 11 December 2014 as trustee for Chorus' longterm incentive plan.

Directors: Clayton Wakefield, Keith Turner and Prue Flacks.

No Chorus LTI Trustee Ltd directors resigned in the year ended 30 June 2016.

#### Director remuneration

The directors of Chorus LTI Trustee Ltd are all directors of Chorus Ltd and do not receive any remuneration in their capacity as directors of Chorus LTI Trustee Ltd.

#### Other subsidiaries

Chorus has no other subsidiaries.

### Bondholder distribution as at 29 July 2016

HOLDING	NUMBER OF HOLDERS	% OF TOTAL HOLDERS	TOTAL NUMBER OF BONDS HELD	% OF BONDS ISSUED
1,001 to 5,000	222	7.95%	1,110,000	0.28%
5,001 to 10,000	519	18.60%	4,984,000	1.25%
10,001 to 100,000	1,860	66.64%	66,036,000	16.51%
100,001 and over	190	6.81%	327,870,000	81.97%
<b>Total</b>	<b>2,791</b>	<b>100%</b>	<b>400,000,000</b>	<b>100%</b>

# Glossary

<b>Backbone network</b>	Fibre cabling and other shared network elements required either in the common areas of multi-dwelling units to connect individual apartments/offices, or to serve premises located along rights of way.	<b>IT</b>	Information Technology.
<b>Backhaul</b>	Is the portion of the network that links local exchanges to other exchanges or retail service provider networks.	<b>Layer 0, 1, 2</b>	Refers to the layers within the Open Systems Interconnection model. Layer 0 is ducts and manholes. Layer 1 is the physical cables and co-location space. Layer 2 is the data link layer including broadband electronics.
<b>Bandwidth fibre access</b>	A fibre service that provides dedicated bandwidth (up to 10Gbps download speed) between customers and their retail service provider's equipment in the local exchange.	<b>LFCs</b>	Local Fibre Companies – refers to the three other organisations the Government has contracted with for the UFB rollout in non-Chorus areas.
<b>Baseband</b>	A technology neutral voice input service that can be bundled with a broadband product or provided on a standalone basis.	<b>Mbps</b>	Megabits per second – a measure of the average rate of data transfer.
<b>Baseband IP</b>	Used by retail service providers to provide a copper voice service from their exchange equipment via Chorus equipment in cabinets or exchanges.	<b>Naked broadband/UBA</b>	Broadband only connections, where the customer does not also take an analogue voice service.
<b>Bitstream 2,3,4</b>	Refers to services defined under the UFB contract. Bitstream 2 and 3 are mass market services (between 30Mbps and 100Mbps downstream speeds). Bitstream 4 is a premium fibre service, which is the equivalent of HSNS fibre for corporate and UFB priority customers.	<b>RBI</b>	Rural Broadband Initiative – refers to the Government programme to improve and enhance broadband coverage in rural areas between 2011 and 2016.
<b>Building block model</b>	Refers to a methodology used for regulating monopoly utilities. Under BBM a regulated supplier's allowed revenue is equal to the sum of the underlying components or 'building blocks', consisting of the return on capital, depreciation, operating expenditure and various other components such as tax.	<b>share</b>	Means an ordinary share in Chorus.
<b>CFH</b>	Crown Fibre Holdings Limited, the Government organisation that manages New Zealand's rollout of Ultra-Fast Broadband infrastructure.	<b>SLES</b>	Sub Loop Extension Service – enables retail service providers to connect a sub loop UCLL line from a cabinet to the exchange.
<b>Chorus</b>	Chorus Limited and subsidiaries.	<b>SLU</b>	Sub Loop Unbundling – where retail service providers use the regulated copper line service available between the premises and cabinet.
<b>Commission</b>	Commerce Commission – the independent Crown Entity whose responsibilities include overseeing the regulation of the telecommunications sector.	<b>TDL</b>	Telecommunications Development Levy – a \$50 million annual levy on telecommunications companies, including Chorus, introduced by Government in FY10 to fund rural broadband. Scheduled to reduce to \$10 million from FY20.
<b>Direct fibre access</b>	Also known as 'dark' fibre, a fibre service that provides a point to point fibre connection and can be used to deliver backhaul connections to mobile sites.	<b>TRL</b>	Telecommunications Regulatory Levy – an annual levy on telecommunications companies, including Chorus, to fund the Commission's costs.
<b>EBITDA</b>	Earnings before interest, income tax, depreciation and amortisation.	<b>TSLRIC</b>	Total Service Long Run Incremental Cost – a forward-looking cost based methodology used by the Commission in its final price review process.
<b>EMTN</b>	European Medium Term Note.	<b>TSO</b>	Telecommunications Services Obligation – a universal service obligation under which Chorus must maintain certain coverage and service on the copper network.
<b>FY</b>	Financial year – twelve months ended 30 June. e.g. FY16 is from 1 July 2015 to 30 June 2016.	<b>UBA</b>	Unbundled Bitstream Access – regulated service that enables retail service providers to use Chorus equipment to deliver broadband to customers.
<b>Gigabit</b>	The equivalent of 1 billion bits. Gigabit Ethernet provides data transfer rates of about 1 gigabit per second.	<b>UCLFS</b>	Unbundled Copper Low Frequency Service – a subset of the baseband voice input service offered over copper, with pricing set at the averaged UCLL price.
<b>Gbps</b>	Gigabits per second. A measure of the average rate of data transfer.	<b>UCLL</b>	Unbundled Copper Local Loop – a regulated service enabling retail service providers to offer voice and broadband services on copper lines using their own electronic equipment in the exchange.
<b>HSNS</b>	High Speed Network Service – a high speed Layer 2 service with dedicated bandwidth on either copper or fibre.	<b>UFB</b>	Ultra-Fast Broadband – refers to the Government programme to build a fibre to the premises network to 75% of New Zealanders by 2020.
<b>IFRS</b>	International Financial Reporting Standards – the rules that the financial statements have to be prepared by.	<b>VDSL</b>	Very High Speed Digital Subscriber Line – a copper-based technology that provides data transmission up to about 100Mbps downstream and 50Mbps upstream.
<b>IP</b>	Internet Protocol.		

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## Forward looking statements and disclaimer

This annual report may contain forward looking statements regarding future events and the future financial performance of Chorus, including forward looking statements regarding industry trends, regulation and the regulatory environment, strategies, capital expenditure, the construction of the UFB network, credit ratings and future financial and operational performance. These forward looking statements are not guarantees or predictions of future performance, and involve known and unknown risks, uncertainties and other factors, many of which are beyond Chorus' control, and which may cause actual results to differ materially from those expressed in the statements

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