PRIMUS TELECOMMUNICATIONS GROUP INC
Form 10-Q
November 09, 2006

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934.

For the quarterly period ended September 30, 2006

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934.

Commission File No. 0-29092

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

(Exact name of registrant as specified in its charter)

Delaware **(State or other jurisdiction of** **incorporation or organization)**	**54-1708481** **(I.R.S. Employer Identification No.)**
7901 Jones Branch Drive, Suite 900, McLean, VA **(Address of principal executive offices)**	**22102** **(Zip Code)**

(703) 902-2800

(Registrant s telephone number, including area code)

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

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

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨

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

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

Class	Outstanding as of October 31, 2006
Common Stock $0.01 par value	113,848,540

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

INDEX TO FORM 10-Q

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

(unaudited)

	Three Months Ended September 30, 2006	Three Months Ended September 30, 2005	Nine Months Ended September 30, 2006	Nine Months Ended September 30, 2005
NET REVENUE	$ 247,702	$ 290,430	$ 769,557	$ 892,055
OPERATING EXPENSES				
Cost of revenue (exclusive of depreciation included below)	158,845	196,488	506,502	592,599
Selling, general and administrative	72,484	92,817	221,455	295,895
Depreciation and amortization	7,003	21,866	41,126	66,001
(Gain) loss on sale or disposal of assets	(205)	12,772	14,302	13,350
Asset impairment write-down			209,248	
Total operating expenses	238,127	323,943	992,633	967,845
INCOME (LOSS) FROM OPERATIONS	9,575	(33,513)	(223,076)	(75,790)
INTEREST EXPENSE	(13,199)	(13,551)	(40,681)	(39,572)
ACCRETION ON DEBT DISCOUNT	222		(1,344)	
CHANGE IN FAIR VALUE OF DERIVATIVES EMBEDDED WITHIN CONVERTIBLE DEBT			5,373	
GAIN (LOSS) ON EARLY EXTINGUISHMENT OR RESTRUCTURING OF DEBT		(4,160)	7,409	(5,865)
INTEREST AND OTHER INCOME	845	780	3,410	2,112
FOREIGN CURRENCY TRANSACTION GAIN (LOSS)	3,896	1,974	8,520	(4,379)
INCOME (LOSS) FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	1,339	(48,470)	(240,389)	(123,494)
INCOME TAX EXPENSE	(1,218)	(2,779)	(3,696)	(7,684)
INCOME (LOSS) FROM CONTINUING OPERATIONS	121	(51,249)	(244,085)	(131,178)
INCOME FROM DISCONTINUED INDIA OPERATIONS, net of tax		602	1,139	1,715
GAIN FROM SALE OF DISCONTINUED INDIA OPERATIONS, net of tax			7,415	
NET INCOME (LOSS)	$ 121	$ (50,647)	$ (235,531)	$ (129,463)
BASIC AND DILUTED INCOME (LOSS) PER COMMON SHARE:				
Income (loss) from continuing operations	$ 0.00	$ (0.52)	$ (2.18)	$ (1.41)
Income from discontinued India operations		0.01		0.02
Gain from sale of discontinued India operations			0.07	
Net income (loss)	$ 0.00	$ (0.51)	$ (2.11)	$ (1.39)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING				
BASIC	113,844	98,640	111,866	93,035
DILUTED	160,779	98,640	111,866	93,035

See notes to consolidated condensed financial statements.

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PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

CONSOLIDATED BALANCE SHEETS

(in thousands, except share amounts)

(unaudited)

	September 30, 2006	December 31, 2005
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 70,828	$ 42,999
Accounts receivable (net of allowance for doubtful accounts receivable of $15,735 and $16,788)	119,419	141,909
Prepaid expenses and other current assets	25,901	31,905
Total current assets	216,148	216,813
RESTRICTED CASH	9,313	10,619
PROPERTY AND EQUIPMENT Net	108,539	285,881
GOODWILL	35,183	85,745
OTHER INTANGIBLE ASSETS Net	3,099	11,392
OTHER ASSETS	29,861	30,639
TOTAL ASSETS	$ 402,143	$ 641,089
LIABILITIES AND STOCKHOLDERS DEFICIT		
CURRENT LIABILITIES:		
Accounts payable	$ 75,556	$ 83,941
Accrued interconnection costs	50,379	64,333
Deferred revenue	19,807	30,037
Accrued expenses and other current liabilities	48,100	31,400
Accrued income taxes	17,379	16,339
Accrued interest	8,936	13,268
Current portion of long-term obligations	41,421	16,092
Total current liabilities	261,578	255,410
LONG-TERM OBLIGATIONS (net of discount of $5,742 and $-0-)	605,520	619,120
OTHER LIABILITIES	1,376	2,893
Total liabilities	868,474	877,423
COMMITMENTS AND CONTINGENCIES (See Note 6.)		
STOCKHOLDERS DEFICIT:		
Preferred stock: not designated, $0.01 par value 1,410,050 shares authorized; none issued and outstanding; Series A and B, $0.01 par value 485,000 shares authorized; none issued and outstanding; Series C, $0.01 par value 559,950 shares authorized; none issued and outstanding		
Common stock, $0.01 par value 300,000,000 shares authorized; 113,848,540 and 105,254,552 shares issued and outstanding	1,138	1,053
Additional paid-in capital	692,876	686,196
Accumulated deficit	(1,085,569)	(850,038)
Accumulated other comprehensive loss	(74,776)	(73,545)
Total stockholders deficit	(466,331)	(236,334)
TOTAL LIABILITIES AND STOCKHOLDERS DEFICIT	$ 402,143	$ 641,089

See notes to consolidated condensed financial statements.

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Nine Months Ended September 30, 2006	2005
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$ (235,531)	$ (129,463)
Adjustments to reconcile net loss to net cash provided by operating activities:		
Provision for doubtful accounts receivable	11,156	17,968
Stock compensation expense	481	
Depreciation and amortization	41,746	66,880
Loss on sale or disposal of assets	6,911	13,364
Asset impairment write-down	209,248	
Accretion of debt discount	1,344	
Equity investment write-off and loss		249
Change in fair value of derivatives embedded within convertible debt	(5,373)	
(Gain) loss on early extinguishment or restructuring of debt	(7,409)	5,865
Minority interest share of loss	(1,595)	(327)
Unrealized foreign currency transaction loss on intercompany and foreign debt	(9,676)	(988)
Changes in assets and liabilities, net of acquisitions:		
Decrease in accounts receivable	15,638	11,858
Decrease in prepaid expenses and other current assets	7,238	5,547
(Increase) decrease in other assets	91	(1,813)
Decrease in accounts payable	(12,536)	(17,912)
Decrease in accrued interconnection costs	(15,850)	(5,087)
Increase, net, in deferred revenue, accrued expenses, accrued income taxes, other current liabilities and other liabilities	7,335	857
Decrease in accrued interest	(4,243)	(4,019)
Net cash provided by (used in) operating activities	8,975	(37,021)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment	(23,926)	(42,522)
Cash from disposition of business, net of cash disposed	12,947	
Cash used for business acquisitions, net of cash acquired	(224)	(226)
Decrease in restricted cash	1,196	5,421
Net cash used in investing activities	(10,007)	(37,327)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of long-term obligations	32,441	109,717
Principal payments on long-term obligations	(9,117)	(16,146)
Proceeds from sale of common stock, net of issuance costs	4,935	221
Net cash provided by financing activities	28,259	93,792
EFFECTS OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	602	(517)
NET CHANGE IN CASH AND CASH EQUIVALENTS	27,829	18,927
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	42,999	49,668
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 70,828	$ 68,595
SUPPLEMENTAL CASH FLOW INFORMATION		
Cash paid for interest	$ 43,197	$ 41,659

Cash paid for taxes	$	2,946	$	2,664
Non-cash investing and financing activities:				
Capital lease additions	$	66	$	809
Property and equipment, accrued in current liabilities	$		$	517
Business acquisition, financed by long-term obligations	$		$	2,064
Settlement of outstanding debt with issuance of common stock	$	1,351	$	17,000
Settlement of outstanding debt with issuance of new convertible debt	$	(27,417)	$	
Issuance of new convertible debt in exchange for convertible subordinated debentures	$	27,481	$	
Settlement of outstanding debt with issuance of new exchangeable debt	$	(54,750)	$	
Issuance of new exchangeable debt in exchange for convertible senior notes	$	47,102	$	

See notes to consolidated condensed financial statements.

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE LOSS

(in thousands)

(unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2006	**2005**	**2006**	**2005**
NET INCOME (LOSS)	$ 121	$ (50,647)	$ (235,531)	$ (129,463)
OTHER COMPREHENSIVE LOSS, NET OF TAX				
Foreign currency translation adjustment	(2,594)	(579)	(883)	(5,423)
Reclassification of foreign currency translation adjustment for loss from the India transaction included in net loss			(349)	
COMPREHENSIVE LOSS	$ (2,473)	$ (51,226)	$ (236,763)	$ (134,886)

See notes to consolidated condensed financial statements.

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

(UNAUDITED)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated condensed financial statements of Primus Telecommunications Group, Incorporated and subsidiaries (the Company or Primus) have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial reporting and Securities and Exchange Commission (SEC) regulations. Certain information and footnote disclosures normally included in the financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such principles and regulations. In the opinion of management, the financial statements reflect all adjustments (all of which are of a normal and recurring nature), which are necessary to present fairly the financial position, results of operations, cash flows and comprehensive loss for the interim periods. The results for the nine months ended September 30, 2006 are not necessarily indicative of the results that may be expected for the year ending December 31, 2006.

Our results for the nine months ended September 30, 2006 and the three and nine months ended September 30, 2005 reflect the activities of our India operations as discontinued operations (see Note 10 Discontinued Operations).

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

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation The consolidated financial statements include the Company s accounts, its wholly-owned subsidiaries and all other subsidiaries over which the Company exerts control. The Company owns 51% of the common stock of Matrix Internet, S.A. (Matrix), 51% of CS Communications Systems GmbH and CS Network GmbH (Citrus) and owned approximately 85% of Direct Internet Limited (DIL) (the India operations) through June 23, 2006, in all of which the Company has or had a controlling interest. In the second quarter of 2006, the Company consummated a share purchase agreement with Videsh Sanchar Nigam Limited (VSNL), whereby VSNL purchased 100% of the stock of DIL. The Company has agreed to purchase an additional 39% of Matrix with the purchase price to be paid in the Company s common stock and is awaiting certain conditions to be met before closing can be completed. All intercompany profits, transactions and balances have been eliminated in consolidation. The Company uses the equity method of accounting for its investment in Bekkoame Internet, Inc. (Bekko).

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

Stock-Based Compensation On January 1, 2006, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 123(R), Share-Based Payments, which addresses the accounting for stock-based payment transactions whereby an entity receives employee services in exchange for equity instruments, including stock options. SFAS No. 123(R) eliminates the ability to account for stock-based compensation transactions using the intrinsic value method under Accounting Principles Board Opinion (APB) No. 25, Accounting for Stock Issued to Employees, and instead generally requires that such transactions be accounted for using a fair-value based method. The Company has elected the modified prospective transition method as permitted under SFAS No. 123(R), and accordingly prior periods have not been restated to reflect the impact of SFAS No. 123(R). The modified prospective transition method requires that stock-based compensation expense be recorded for all new and unvested stock options that are ultimately expected to vest as the requisite service is rendered beginning on January 1, 2006. Stock-based compensation for awards granted prior to January 1, 2006 is based upon the grant-date fair value of such compensation as determined under the pro forma provisions of SFAS No. 123, Accounting for Stock-Based Compensation. The Company issues new shares of common stock upon the exercise of stock options.

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

The Company recorded an incremental $246 thousand and $481 thousand of stock-based compensation expense during the three months and nine months ended September 30, 2006, respectively, as a result of the adoption of SFAS No. 123(R).

Prior to the adoption on January 1, 2006 of SFAS No. 123(R), the Company used the intrinsic value method to account for these plans under the recognition and measurement principles of APB Opinion No. 25 and related interpretations. The following table illustrates the effect on net loss and loss per share if the Company had applied the fair value recognition provisions of SFAS No. 123, Accounting for Stock-Based Compensation, to stock-based employee compensation during 2005.

	For the Three Months Ended September 30, 2005		
	As Determined Under SFAS No. 123(R)	As Reported Under APB No. 25	Difference
Loss from continuing operations	$ (52,196)	$ (51,249)	$ (947)
Income from discontinued India operations	602	602	
Net loss	$ (51,594)	$ (50,647)	$ (947)
Basic income (loss) per share:			
Loss from continuing operations	$ (0.53)	$ (0.52)	$ (0.01)
Income from discontinued operations	0.01	0.01	
Net loss	$ (0.52)	$ (0.51)	$ (0.01)
Diluted income (loss) per share:			
Loss from continuing operations	$ (0.53)	$ (0.52)	$ (0.01)
Income from discontinued operations	0.01	0.01	
Net loss	$ (0.52)	$ (0.51)	$ (0.01)

	For the Nine Months Ended September 30, 2005		
	As Determined Under SFAS No. 123(R)	As Reported Under APB No. 25	Difference
Loss from continuing operations	$ (134,002)	$ (131,178)	$ (2,824)
Income from discontinued India operations	1,715	1,715	
Net loss	$ (132,287)	$ (129,463)	$ (2,824)
Basic income (loss) per share:			
Loss from continuing operations	$ (1.44)	$ (1.41)	$ (0.03)
Income from discontinued operations	0.02	0.02	
Net loss	$ (1.42)	$ (1.39)	$ (0.03)
Diluted income (loss) per share:			
Loss from continuing operations	$ (1.44)	$ (1.41)	$ (0.03)
Income from discontinued operations	0.02	0.02	
Net loss	$ (1.42)	$ (1.39)	$ (0.03)

The weighted average fair value, under SFAS No. 123(R), at date of grant for options granted during the three and nine months ended September 30, 2006 was $0.29 and $0.43 per option, respectively. The weighted average fair value, under SFAS No. 123(R), at date of grant for options granted during the three and nine months ended September 30, 2005 was $0.28 and $0.43, respectively. The fair value, under SFAS No. 123(R), of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	For the Three Months Ended September 30,	
	2006	2005
Expected dividend yield	0%	0%
Expected stock price volatility	94.9%	72.1%
Risk-free interest rate	5.1%	4.1%
Expected option term	4 years	4 years

Under SFAS No. 123(R), the Company was required to apply expense recognition provisions beginning January 1, 2006. As of September 30, 2006, the Company had 1.6 million unvested awards outstanding of which $0.7 million of compensation expense will be recognized over the weighted average remaining vesting period of 2.2 years.

On December 21, 2005, the Company accelerated the vesting of certain unvested stock options previously awarded under the Company s Equity Incentive Plan and Director Plan. The Company took this action because the future costs to be recognized if this action were not taken were disproportionate to the retention value of the stock options. As a result of this action, stock options to purchase up to 1.5 million shares of common stock, which would otherwise have vested over the next three years, became exercisable effective December 21, 2005. These stock options have exercise prices ranging from $1.61 to $6.30 per share. Based upon the closing stock price for the Company s common stock of $0.82 per share on December 21, 2005, all of these stock options were under water or out-of-the-money. Of the stock options whose vesting was accelerated, 0.6 million stock options were held by executive officers and 30,000 stock options were held by non-employee directors. Outstanding unvested stock options to purchase 1.5 million shares of the Company s common stock, with per share exercise prices ranging from $0.62 to $0.92, were not accelerated.

Derivative Instruments The Company does not hold or issue derivative instruments for trading purposes. During the three months ended March 31, 2006, the Company had entered into financing arrangements that contained embedded derivative features due to the Company having insufficient authorized shares. The Company accounted for these arrangements in accordance with SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities , and Emerging Issues Task Force (EITF) Issue No. 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company s Own Stock , as well as related interpretations of these standards. The Company bifurcated embedded derivatives that were not clearly and closely related to the host contract and recorded them as a liability in its balance sheet at their estimated fair value. Changes in their estimated fair value of $5.4 million were recognized in earnings during the period of change. Since June 20, 2006, when authorization for sufficient authorized shares was obtained, the feature that established the embedded derivative no longer exists. The fair value of the embedded derivative at June 20, 2006, was added back to the debt balance.

The Company estimated the fair value of its embedded derivatives using available market information and appropriate valuation methodologies. These embedded derivatives derived their value primarily based on changes in the price and volatility of the Company s common stock. Considerable judgment is required in interpreting market data to develop the estimates of fair value.

Accounting for derivatives was based upon valuations of derivative instruments determined using various valuation techniques including Black-Scholes and binomial pricing methodologies. The Company considered such valuations to be significant estimates.

New Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R), SFAS No. 158 requires recognition of the over- or underfunded status of defined benefit postretirement plans as an asset or liability in the statement of financial position and to recognize changes in that funded status in comprehensive income in the year in which the changes occur. SFAS No. 158 also requires measurement of the funded status of a plan as of the date of the statement of financial position. SFAS No. 158 is effective for recognition of the funded status of the benefit plans for fiscal years ending after December 15, 2006 and is effective for the measurement date provisions for fiscal years ending after December 15, 2008. The Company anticipates that the adoption of this standard will not have a material impact on its results of operations, financial position and cash flows.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurement. SFAS No. 157 does not require new fair value measurements and the Company does not expect the application of this standard to change our current practices. The provisions of SFAS No. 157 are effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company is currently assessing the impact that adoption of SFAS No. 157 will have on its results of operations, financial position and cash flows.

In July 2006, the FASB issued FASB Interpretation (FIN) No. 48, Accounting for Uncertainty in Income Taxes, which is effective for fiscal years beginning after December 15, 2006. FIN No. 48 clarifies the accounting for uncertainty in income taxes recognized in the financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. This Interpretation prescribes a comprehensive model for how a company should recognize, measure, present, and disclose in its financial statements uncertain tax positions that the company has taken or expects to take on a tax return. The Company is currently evaluating the impact of adopting FIN No. 48 on its results of operations, financial position and cash flows.

In February 2006, the FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments, an amendment of FASB Statements No. 133 and 140. SFAS No. 155 clarifies certain issues relating to embedded derivatives and beneficial interests in securitized financial assets. The provisions of SFAS No. 155 are effective for all financial instruments acquired or issued after fiscal years beginning after September 15, 2006. The Company is currently assessing the impact that the adoption of SFAS 155 will have on its results of operations, financial position and cash flows.

3. GOODWILL AND OTHER INTANGIBLE ASSETS

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

	As of September 30, 2006			As of December 31, 2005		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value	Gross Carrying Amount	Accumulated Amortization	Net Book Value
Customer lists	$ 3,541	$ (473)	$ 3,068	$ 190,370	$ (179,863)	$ 10,507
Brand name acquired				3,420	(3,148)	272
Other	257	(226)	31	2,400	(1,787)	613
Total	$ 3,798	$ (699)	$ 3,099	$ 196,190	$ (184,798)	$ 11,392

Amortization expense for customer lists, brand name and other intangible assets for the three months ended September 30, 2006 and 2005 was $0.7 million and $3.9 million, respectively. Amortization expense for customer lists, brand name and other intangible assets for the nine months ended September 30, 2006 and 2005 was $4.3 million and $12.7 million, respectively. The Company expects amortization expense for customer lists, brand name and other intangible assets for the remainder of 2006 and the fiscal years ended December 31, 2007, 2008 and 2009 to be approximately $0.5 million, $1.5 million, $0.8 million and $0.3 million, respectively.

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

	As of September 30, 2006	As of December 31, 2005
Goodwill	$ 35,183	$ 85,745

The changes in the carrying amount of goodwill for the nine months ended September 30, 2006 are as follows (in thousands):

	United States and Other	Canada	Europe	Asia-Pacific	Total
Balance as of January 1, 2006	$ 36,771	$ 31,427	$ 1,822	$ 15,725	$ 85,745
Goodwill impairment write-down	(21,769)	(19,337)	(1,927)	(8,880)	(51,913)
Sale of discontinued operations				(723)	(723)
Effect of change in foreign currency exchange rates	230	1,521	105	218	2,074
Balance as of September 30, 2006	$ 15,232	$ 13,611	$	$ 6,340	$ 35,183

4. LONG-TERM OBLIGATIONS

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

	As of September 30, 2006	As of December 31, 2005
Obligations under capital leases	$ 6,449	$ 7,612
Leased fiber capacity	13,505	19,717
Senior secured term loan facility	98,500	99,250
Financing facility and other	32,633	17,454
Senior notes	306,560	309,060
Convertible senior notes	75,757	132,000
Exchangeable senior notes	67,603	
Step up convertible subordinated debentures	23,232	
Convertible subordinated debentures	22,702	50,119
Subtotal	646,941	635,212
Less: Current portion of long-term obligations	(41,421)	(16,092)
Total long-term obligations	$ 605,520	$ 619,120

Payments of principal and interest were due as follows (in thousands):

Year Ending December 31,	Vendor Financing	Senior Secured Term Loan Facility (1)	Financing Facility and Other	Senior Notes	Convertible and Exchangeable Senior Notes (2) (3)	Step Up Convertible Subordinated Debentures	Convertible Subordinated Debentures	Total
2006 (as of September 30, 2006)	$ 2,390	$ 3,110	$ 961	$ 4,562	$ 1,424	$	$	$ 12,447
2007	12,494	12,363	5,752	28,324	5,713	1,832	23,355	89,833
2008	3,311	12,247	29,490	28,324	5,713	2,107		81,192
2009	1,605	12,131	28	99,884	5,713	29,679		149,040
2010	2,240	12,015	28	19,200	137,879			171,362
Thereafter		94,250	118	302,200				396,568
Total Minimum Principal & Interest Payments	22,040	146,116	36,377	482,494	156,442	33,618	23,355	900,442
Less: Amount Representing Interest	(2,086)	(47,616)	(3,744)	(175,934)	(22,869)	(6,137)	(653)	(259,039)
Face Value of Long-Term Obligations	19,954	98,500	32,633	306,560	133,573	27,481	22,702	641,403
Less: Amount Representing Discount					(1,493)	(4,249)		(5,742)
Add: Exchangeable Notes Interest Treated as Long-Term Obligations (3)					11,280			11,280
Book Value of Long Term Obligations	$ 19,954	$ 98,500	$ 32,633	$ 306,560	$ 143,360	$ 23,232	$ 22,702	$ 646,941

(1) For preparation of this table, we have assumed the interest rate of the Senior Secured Term Loan Facility to be 11.9%, which is the interest rate at September 30, 2006.

(2) For preparation of this table, we have assumed that the maturity date for the 5% Exchangeable Senior Notes is June 30, 2010 and will not be accelerated to June 30, 2009.

(3) For preparation of this table, we have shown separately the cash interest payments of PTHI s 5% Exchangeable Senior Notes due June 2009 (5% Exchangeable Senior Notes) as a portion of long-term obligations (see *Senior Notes, Convertible Senior Notes, Exchangeable Senior Notes, Step Up Convertible Subordinated Debentures and Convertible Subordinated Debentures* below).

The indentures governing the senior notes, senior secured term loan facility, convertible senior notes, exchangeable senior notes, step up convertible subordinated debentures and convertible subordinated debentures, as well as other credit arrangements, contain certain financial and other covenants which, among other things, will restrict the Company s ability to incur further indebtedness and make certain payments, including the payment of dividends and repurchase of subordinated debt held by the Company s subsidiaries. The Company was in compliance with the above covenants at September 30, 2006.

Senior Secured Term Loan Facility

In February 2005, a direct wholly-owned subsidiary of the Company, Primus Telecommunications Holding, Inc. (PTHI), completed a six-year, $100 million senior secured term loan facility (the Facility). Each borrowing made under the Facility may be, at the election of PTHI at the time of the borrowing, a London Inter-Bank Offered Rate (LIBOR) loan (which will bear interest at a rate equal to LIBOR + 6.50%), or a base rate loan (which will bear interest at a rate equal to the greater of the prime rate plus 5.50% or the federal funds effective rate plus 6.0%). The interest rate at September 30, 2006 was 11.9%. The Facility contains no financial maintenance covenants. The Company borrowed $100 million under this facility in February 2005. The Facility will be repaid in 24 quarterly installments, which began on June 30, 2005, at a rate of one percent of the original principal per year over the next five years and nine months, and the remaining balance repaid on the sixth anniversary date of the Facility, with early redemption at a premium to par at PTHI s option at any time after February 18, 2006. The Facility is guaranteed by the Company and certain of PTHI s subsidiaries and is secured by certain assets of PTHI and its guarantor subsidiaries.

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

In the second quarter 2006, the Company completed the exchange of $54.8 million principal amount of the Company s 3 3/4% convertible senior notes due 2010 (2003 Convertible Senior Notes) and $20.5 million in cash for $56.3 million principal amount of the 5% Exchangeable Senior Notes. This exchange has been deemed a troubled debt restructuring, and accordingly, has been accounted for as a modification of debt, with total future cash payments of $67.6 million being recorded in long-term obligations. The Company recognized a gain on restructuring of debt of $4.8 million in connection with this exchange, including the expensing of $2.9 million of financing costs. The 5% Exchangeable Senior Notes will mature on June 30, 2010, subject to an accelerated maturity of June 30, 2009 at the option of the holders if the Company does not increase its equity (through designated transactions) in the aggregate of $25 million during the three years following issuance of the senior notes. Interest of the 5% Exchangeable Senior Notes will be paid at the rate of 5% per annum on each June 30 and December 30, beginning on December 30, 2006. Under certain circumstances, the Company may elect to make interest payments in shares of common stock, although the holders of the 5% Exchangeable Senior Notes will be entitled to receive the first two semi-annual interest payments wholly in cash. The 5% Exchangeable Senior Notes are exchangeable, in the aggregate, into 46,935,833 shares of the Company s common stock at a conversion price of $1.20 per share of common stock, subject to adjustment. If the closing bid price of the Company common stock, for at least 20 trading days in any consecutive 30 trading-day period, exceeds 150% of the conversion price then in effect, the Company may elect to exchange the senior notes for shares of the Company common stock at the conversion price, subject to certain conditions, including that no more than 50% of the senior notes may be exchanged by the Company within any 30-day period. In the event of a change in control, as defined, the holders may require the Company to repurchase the 5% Exchangeable Senior Notes at which time the Company has the option to settle in cash or common stock at an adjusted conversion price.

In the first quarter 2006, the Company completed the exchange of $27.4 million principal amount of the Company s 5 3/4% convertible subordinated debentures due 2007 (2000 Convertible Subordinated Debentures) for $27.5 million principal amount of the Company s step up convertible subordinated debentures due August 2009 (Step Up Convertible Subordinated Debentures) through two transactions. The Company recognized a gain on early extinguishment of debt of $1.5 million in connection with this exchange. The Step Up Convertible

Subordinated Debentures will mature on August 15, 2009. Interest will be payable from February 27, 2006 to December 31, 2006 at the rate of 6% per annum; from January 1, 2007 to December 31, 2007 at the rate of 7% per annum; and from January 1, 2008 to maturity at the rate of 8% per annum. Accrued interest will be paid each February 15 and August 15, beginning August 15, 2006, to holders of record on the preceding February 1 and August 1, respectively. The Step Up Convertible Subordinated Debentures are convertible into the Company s common stock at a conversion price of $1.187 per share of common stock through August 15, 2009. The Step Up Convertible Subordinated Debentures are convertible in the aggregate into 23,151,643 shares of the Company s common stock. The Indenture permits the Company, at its sole option, to require conversion if the Company s stock trades at 150% of the conversion price for at least 20 days within a 30 day period, subject to certain conditions, including that no more than 25% of the notes may be exchanged within any 30 day trading period. In the event of a change in control, as defined, the holders may put the instrument to the Company at which time the Company has the option to settle in cash or common stock at an adjusted conversion price. The Step Up Convertible Subordinated Debentures are subordinated to all indebtedness of the Company, except for other subordinated indebtedness.

At the time of issuance of the Step Up Convertible Subordinated Debentures, the Company did not have sufficient authorized and unissued shares of common stock to satisfy exercise and conversion of all of its convertible instruments. Accordingly, the Company determined that the Step Up Convertible Subordinated Debentures, the 2000 Convertible Subordinated Debentures and the 2003 Convertible Senior Notes were hybrid instruments with characteristics of a debt host agreement and contained embedded derivative features that had characteristics and risks that were not clearly and closely associated with the debt host. In the first quarter 2006, the conversion options were determined to be derivative instruments to be bifurcated and recorded as a current liability at fair value. In the second quarter 2006, the Company s shareholders voted to approve alternative proposals to authorize an amendment to the Company s Certificate of Incorporation to affect a one-for-ten reverse stock split or to authorize an amendment of the Company s Certificate of Incorporation allowing an increase of authorized Common Stock from 150,000,000 to 300,000,000. Either authorization ensured the Company would have the ability to control whether it has sufficient authorized and unissued shares of common stock to satisfy exercise and conversion of all of its convertible instruments. Therefore, the Company determined that the Step Up Convertible Subordinated Debentures, the 2000 Convertible Subordinated Debentures and the 2003 Convertible Senior Notes did not contain embedded derivative features as of the date of the shareholder vote, June 20, 2006, and added back the June 20, 2006 fair value of the embedded derivative into the debt balance. On July 27, 2006, the Board of Directors determined to increase the authorized shares to 300,000,000.

The Company recorded a corresponding debt discount to the Step Up Convertible Subordinated Debentures and the 2003 Convertible Senior Notes in the amount of the fair value of the embedded derivative at the issue date. An additional debt discount of $1.7 million was recorded for the Step Up Convertible Subordinated Debentures to bring the carrying value to fair value. The carrying value of the Step Up Convertible Subordinated Debentures at issuance was approximately $14.3 million, and the carrying value of the 2003 Convertible Senior Notes at issuance of the Step Up Convertible Subordinated Debentures was approximately $127.8 million. The Company is accreting the difference between the face values of the Step Up Convertible Subordinated Debentures and the 2003 Convertible Senior Notes and the corresponding carrying values to interest expense under the effective interest method on a monthly basis over the lives of the Step Up Convertible Subordinated Debentures and the 2003 Convertible Senior Notes. At September 30, 2006, the carrying value of the Step Up Convertible Subordinated Debentures (face value of $27.5 million) was $23.2 million, and the carrying value of the 2003 Convertible Senior Notes (face value of $77.3 million) was $75.8 million. The effective interest rate of the Step Up Convertible Subordinated Debentures and the 2003 Convertible Senior Notes at September 30, 2006 was 14.0% and 5.4%, respectively.

In January 2004, PTHI, a direct, wholly-owned subsidiary of the Company, completed the sale of $240 million in aggregate principal amount of 8% senior notes due 2014 (2004 Senior Notes) with semi-annual interest payments due on January 15th and July 15th, with early redemption at a premium to par at PTHI s option at any time after January 15, 2009. The Company recorded $6.7 million in costs associated with the issuance of

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the 2004 Senior Notes, which have been recorded as deferred financing costs in other assets. The effective interest rate at September 30, 2006 was 8.4%. During specified periods, PTHI may redeem up to 35% of the original aggregate principal amount with the net cash proceeds of certain equity offerings of the Company. During the year ended December 31, 2004, the Company reduced $5.0 million principal balance of the 2004 Senior Notes through open market purchases.

In September 2003, the Company completed the sale of $132 million in aggregate principal amount of 2003 Convertible Senior Notes with semi-annual interest payments due on March 15th and September 15th. The Company recorded $5.2 million in costs associated with the issuance of the 2003 Convertible Senior Notes, which have been recorded as deferred financing costs in other assets. Holders of these notes may convert their notes into the Company s common stock at any time prior to maturity at an initial conversion price of $9.3234 per share, which is equivalent to an initial conversion rate of 107.257 shares per $1,000 principal amount of the notes, subject to adjustment in certain circumstances. The outstanding notes are convertible in the aggregate into 8,285,603 shares of the Company s common stock. In the event of a change in control, as defined, the holders may put the instrument to the Company at which time the Company has the option to settle in cash or common stock at an adjusted conversion price. In the second quarter 2006, the Company restructured $54.8 million principal amount of 2003 Convertible Senior Notes; see prior disclosure regarding the 5% Exchangeable Senior Notes within this footnote.

In February 2000, the Company completed the sale of $250 million in aggregate principal amount of 2000 Convertible Subordinated Debentures with semi-annual interest payments due on February 15th and August 15th. On March 13, 2000, the Company announced that the initial purchasers of the 2000 Convertible Subordinated Debentures had exercised their $50 million over-allotment option granted pursuant to a purchase agreement dated February 17, 2000. During the years ended December 31, 2001 and 2000, the Company reduced $36.4 million principal balance of the debentures through open market purchases and $192.5 million principal balance through exchanges for its common stock. The principal that was exchanged for common stock was retired upon conversion and in February 2002, the Company retired all of the 2000 Convertible Subordinated Debentures that it had previously purchased in December 2000 and January 2001. The retired principal had been held by the Company as treasury bonds and had been recorded as a reduction of long-term obligations. During the year ended December 31, 2004, the Company retired $4.0 million principal amount of the 2000 Convertible Subordinated Debentures through open market purchases. During the year ended December 31, 2005, the Company exchanged 9,820,000 shares of the Company s common stock for the extinguishment of $17.0 million principal amount of these debentures. In accordance with SFAS No. 84, Induced Conversion of Convertible Debt, the Company recognized an induced conversion expense of $6.1 million in connection with this conversion. During the quarter ended March 31, 2006, the Company exchanged $27.4 million of the 2000 Convertible Subordinated Debentures for $27.5 million principal amount of the Company s Step Up Convertible Subordinated Debentures. The remaining debentures are convertible at a conversion price of $49.7913 per share in the aggregate into 455,943 shares of the Company s common stock. In the event of a change in control, as defined, the holders may put the instrument to the Company at which time the Company has the option to settle in cash or common stock at an adjusted conversion price.

In October 1999, the Company completed the sale of $250 million in aggregate principal amount of 12.75% senior notes due 2009 (the October 1999 Senior Notes). The October 1999 Senior Notes are due October 15, 2009, with semi-annual interest payments due on October 15th and April 15th with early redemption at a premium to par at the Company s option at any time after October 15, 2004. During the years ended December 31, 2002, 2001 and 2000, the Company reduced the principal balance of these senior notes through open market purchases. In June and September 2002, the Company retired all of the October 1999 Senior Notes that it had previously purchased in the principal amount of $134.3 million in aggregate. The retired principal had been held by the Company as treasury bonds and had been recorded as a reduction of long-term obligations. During the year ended December 31, 2004, the Company retired $33.0 million principal amount of the October 1999 Senior Notes through open market purchases. During the year ended December 31, 2005, the Company exchanged 5,165,175 shares of the Company s common stock for the extinguishment of $8.6 million principal amount of these senior notes. During the quarter ended March 31, 2006, the Company exchanged 1,825,000 shares of the Company s common stock for the extinguishment of $2.5 million principal amount of these senior notes.

Leased Fiber Capacity

Beginning September 30, 2001, the Company accepted delivery of fiber optic capacity on an indefeasible rights of use (IRU) basis from Southern Cross Cables Limited (SCCL). The Company and SCCL entered into an arrangement financing the capacity purchase. During the three months ended December 31, 2001, the Company renegotiated the payment terms with SCCL. The effective interest rate on current borrowings is 7.4%. The Company agreed to purchase $12.2 million of additional fiber optic capacity from SCCL under the IRU agreement. The Company has fulfilled the total purchase obligation and made additional purchases of $3.8 million in 2004. At September 30, 2006 and December 31, 2005, the Company had a liability recorded under this agreement in the amount of $6.0 million and $10.7 million, respectively.

In December 2000, the Company entered into a financing arrangement to purchase fiber optic capacity in Australia for 51.1 million AUD ($28.5 million at December 31, 2000) from Optus Networks Pty. Limited. As of December 31, 2001, the Company had fulfilled the total purchase obligation. The Company signed a promissory note payable over a four-year term ending in April 2005 bearing interest at a rate of 14.31%. During the three months ended June 30, 2003, the Company renegotiated the payment terms extending the payment schedule through March 2007, and lowering the interest rate to 10.2%. At September 30, 2006 and December 31, 2005, the Company had a liability recorded in the amount of $7.5 million (10.1 million AUD) and $9.0 million (12.4 million AUD), respectively. In October 2006, the Company renegotiated the payment terms of its promissory note payable to Optus Networks Pty. Limited to defer principal payments from April 2006 through December 2006. The debt will mature in March 2007 and the Company is obligated to pay an aggregate $7.5 million (10.1 million AUD) in three equal monthly principal payments in the first quarter 2007. The interest rate remains 10.2%, and the interest payments continue monthly. See Note 13 Subsequent Events .

Equipment Financing and Other Long-Term Obligations

In November 2005, Primus Australia entered into a financing arrangement with Alleasing Finance Australia United for network equipment. Payments will be made over a five-year term ending October 2010. The effective interest rate on the current borrowing is 9.3%. At September 30, 2006 and December 31, 2005, the Company had a liability recorded under this agreement in the amount of $5.1 million (6.8 million AUD) and $6.1 million (8.4 million AUD), respectively.

In April 2004, Primus Canada entered into a loan agreement with a Canadian financial institution. The agreement provided for a $37.8 million (42 million CAD) two-year non-revolving term loan credit facility, bearing an interest rate of 7.75%. The agreement allows the proceeds to be used for general corporate purposes of the Company and is secured by the assets of Primus Canada s operations. In October 2004, Primus Canada signed an amendment to the April 2004 loan agreement that extended the maturity date one year to April 2007. In January 2006, Primus Canada entered into an Amended and Restated Loan Agreement that extended the maturity date one year to April 2008. The agreement is now a four-year non-revolving term loan credit facility bearing an interest rate of 7.75%. The new agreement reduced the maximum loan balance from $37.8 million (42 million CAD) to $28.8 million (32 million CAD) and established quarterly principal payments of $0.9 million (1 million CAD) commencing in April 2007. In February 2006, the Company drew the remaining $15.3 million (17 million CAD) available under the amended loan facility. At September 30, 2006 and December 31, 2005, the Company had an outstanding liability of $28.8 million (32 million CAD) and $12.8 million (15.0 million CAD), respectively. An affiliate of Primus Canada has an additional loan facility agreement with the Canadian financial institution and had a liability under this facility of $2.7 million (3.0 million CAD) and $2.6 million (3.0 million CAD) at September 30, 2006 and December 31, 2005, respectively.

5. ASSET IMPAIRMENT

In the second quarter 2006, pursuant to SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets, the Company identified certain indications of impairment. The overall deterioration in economic conditions within the telecommunications industry, including certain pricing actions enacted by incumbent carriers, during the first half of 2006 led the Company to believe that the fair value of certain long-lived assets had decreased significantly. Because of the impairment identified under the guidance of SFAS No. 144, the Company performed an analysis under SFAS No. 142, Goodwill and Other Intangible Assets. Through that evaluation, the Company determined that an additional $0.8 million impairment (which is included in the figures below) to goodwill was required in Europe.

Based on the Company s evaluation, it was determined that the estimated future cash flows were less than the carrying value of its long-lived assets. The Company s assets were evaluated as a single asset group, because of the nature of the cash flows being inseparable within a global telecommunications company. Therefore, the impairment was applied equally across the entire asset group. Accordingly, during the second quarter 2006, the Company adjusted the carrying value of its long-lived assets, including property and equipment and intangible assets, to their estimated fair value of $143.6 million. This adjustment resulted in an asset impairment write-down of $209.2 million, or $1.87 per share, consisting of the following specific asset write-downs: $151.8 million in property and equipment, $52.1 million in goodwill and $5.3 million in customer lists and other intangible assets. The estimated fair value of the Company s assets was based on the present value of estimated future cash flows using a discount rate commensurate with the risks involved.

The following table outlines the Company s asset impairment write-down by segment (in thousands):

		Three months ended June 30, 2006
United States and Other		
United States	$	51,688
Other		2,819
Total United States and Other		54,507
Canada		
Canada		55,228
Total Canada		55,228
Europe		
United Kingdom		9,991
Germany		1,430
Netherlands		1,677
Other		5,800
Total Europe		18,898
Asia-Pacific		
Australia		76,843
Other		3,772
Total Asia-Pacific		80,615
Total	$	209,248

6. COMMITMENTS AND CONTINGENCIES

Future minimum lease payments under capital leases and leased fiber capacity financing (Vendor Financing), purchase obligations and non-cancelable operating leases as of September 30, 2006 are as follows (in thousands):

Year Ending December 31,	Vendor Financing	Purchase Obligations	Operating Leases	Total
2006 (from October 1 through December 31)	$ 2,390	$ 867	$ 3,636	$ 6,893
2007	12,494	1,385	11,575	25,454
2008	3,311		8,120	11,431
2009	1,605		5,868	7,473
2010	2,240		3,671	5,911
Thereafter			4,431	4,431
Total minimum lease payments	22,040	2,252	37,301	61,593
Less: Amount representing interest	(2,086)			(2,086)
	$ 19,954	$ 2,252	$ 37,301	$ 59,507

The Company has contractual obligations to utilize an external vendor for certain back-office support functions and to utilize network facilities from certain carriers with terms greater than one year. The Company does not purchase or commit to purchase quantities in excess of normal usage or amounts that cannot be used within the contract term or at rates below or above market value. The Company made purchases under purchase commitments of $2.6 million and $7.1 million for the three months ended September 30, 2006 and 2005, respectively. The Company made purchases under purchase commitments of $8.7 million and $21.9 million for the nine months ended September 30, 2006 and 2005, respectively.

Rent expense under operating leases was $4.1 million and $4.5 million for the three months ended September 30, 2006 and 2005, respectively. Rent expense under operating leases was $12.7 million and $14.2 million for the nine months ended September 30, 2006 and 2005, respectively.

Litigation

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

7. SHARE-BASED COMPENSATION

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

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

On December 21, 2005, the Company accelerated the vesting of certain unvested stock options previously awarded under the Company s Equity Incentive Plan and Director Plan. The Company took this action because the future costs to be recognized if this action were not taken were disproportionate to the retention value of the stock options. As a result of this action, stock options to purchase up to 1.5 million shares of common stock, which would otherwise have vested over the next three years, became exercisable effective December 21, 2005. These stock options have exercise prices ranging from $1.61 to $6.30 per share. Based upon the closing stock price for the Company s common stock of $0.82 per share on December 21, 2005, all of these stock options were under water or out-of-the-money. Of the stock options whose vesting was accelerated, 0.6 million stock options were held by executive officers and 30,000 stock options were held by non-employee directors. Outstanding unvested stock options to purchase 1.5 million shares of the Company s common stock, with per share exercise prices ranging from $0.62 to $0.92, were not accelerated.

A summary of stock option activity during the nine months ended September 30 is as follows:

	2006		2005	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Options outstanding January 1	9,312,945	$ 2.36	8,606,888	$ 2.92
Granted	797,500	$ 0.76	60,000	$ 0.95
Exercised		$	(34,250)	$ 1.57
Forfeitures	(1,804,638)	$ 2.44	(532,527)	$ 6.57
Outstanding September 30	8,305,807	$ 2.18	8,100,111	$ 2.68
Eligible for exercise September 30	6,725,234		6,250,703	

The following table summarizes information about stock options outstanding at September 30, 2006:

	Options Outstanding				Options Exercisable		
Range of Option Prices	Total Outstanding	Weighted Average Remaining Life in Years	Weighted Average Exercise Price	Intrinsic Value	Total Exercisable	Weighted Average Exercise Price	Intrinsic Value
$0.53 to $0.76	292,167	5.93	$ 0.63	$	230,833	$ 0.63	$
$0.77	500,000	9.34	$ 0.77		83,333	$ 0.77	
$0.79 to $0.88	190,000	7.96	$ 0.86		54,166	$ 0.83	
$0.90	824,140	4.77	$ 0.90		824,140	$ 0.90	
$0.92	1,174,331	9.10	$ 0.92		207,593	$ 0.92	
$0.93 to $1.61	49,500	8.06	$ 1.26		49,500	$ 1.26	
$1.65	1,685,836	6.22	$ 1.65		1,685,836	$ 1.65	
$1.80 to $2.38	1,982,133	6.07	$ 1.98		1,982,133	$ 1.98	
$3.03 to $6.30	1,571,000	7.65	$ 5.09		1,571,000	$ 5.09	
$12.31 to $17.44	20,900	2.98	$ 14.54		20,900	$ 14.54	
$31.94 to $33.38	15,800	3.59	$ 33.38		15,800	$ 33.38	

8,305,807	$	6,725,234	$

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In December 1998, the Company established the 1998 Restricted Stock Plan (the Restricted Plan) to facilitate the grant of restricted stock to selected individuals (excluding executive officers and directors of the Company) who contribute to the development and success of the Company. The total number of shares of common stock that may be granted under the Restricted Plan is 750,000. The Company did not issue any restricted stock under the Restricted Plan for the nine months ended September 30, 2006 and 2005. As of September 30, 2006, 54,000 shares have been issued and none are considered restricted.

8. GAIN OR LOSS ON EARLY EXTINGUISHMENT OR RESTRUCTURING OF DEBT

In 2006, the Company issued $56.3 million principal amount of PTHI s 5% Exchangeable Senior Notes in exchange for $20.5 million of cash and the retirement of $54.8 million principal amount of the Company s 2003 Convertible Notes. This exchange has been accounted for as a troubled debt restructuring, resulting in $11.3 million of future cash payments being recognized as long-term obligations and a gain on restructuring of debt of $4.8 million.

In March 2006, the Company exchanged $27.4 million principal amount of the Company s 2000 Convertible Subordinated Debentures for $27.5 million principal amount of the Company s 2006 Step Up Convertible Subordinated Debentures resulting in a gain on early extinguishment of debt of $1.5 million including the write-off of related deferred financing costs. In January 2006, the Company exchanged 1,825,000 shares of the Company s common stock for the extinguishment of $2.5 million in principal amount of the October 1999 Senior Notes resulting in a $1.2 million gain on early extinguishment of debt including the write-off of related deferred financing costs.

9. OPERATING SEGMENT AND RELATED INFORMATION

The Company has four reportable operating segments based on management s organization of the enterprise into geographic areas United States and Other, Canada, Europe and Asia-Pacific. The Company evaluates the performance of its segments and allocates resources to them based upon net revenue and income (loss) from operations. The accounting policies of the segments are the same as those described in the summary of significant accounting policies. Net revenue by reportable segment is reported on the basis of where services are provided. The Company has no single customer representing greater than 10% of its revenues. Operations and assets of the United States and Other segment include shared corporate functions and assets, which the Company does not allocate to its other geographic segments for management reporting purposes.

Summary information with respect to the Company s segments is as follows and is shown net of discontinued operations for net revenue and income (loss) from operations (in thousands):

	Three months ended September 30, 2006	Three months ended September 30, 2005	Nine months ended September 30, 2006	Nine months ended September 30, 2005
Net Revenue				
United States and Other				
United States	$ 48,572	$ 47,420	$ 142,552	$ 153,178
Other	1,034	883	3,009	2,395
Total United States and Other	49,606	48,303	145,561	155,573
Canada				
Canada	68,251	67,189	208,935	193,058
Total Canada	68,251	67,189	208,935	193,058
Europe				
United Kingdom	19,876	22,397	63,203	93,651
Germany	12,393	14,232	35,352	40,859
Netherlands	4,424	32,555	31,613	70,967
Other	15,396	19,712	47,235	66,653
Total Europe	52,089	88,896	177,403	272,130
Asia-Pacific				
Australia	76,243	83,221	232,447	262,879
Other	1,513	2,821	5,211	8,415
Total Asia-Pacific	77,756	86,042	237,658	271,294
Total net revenue	$ 247,702	$ 290,430	$ 769,557	$ 892,055
Income (Loss) from Operations				
United States and Other	$ (1,900)	$ (15,036)	$ (81,689)	$ (51,597)
Canada	11,639	5,991	(27,890)	18,107
Europe	(2,831)	(17,786)	(36,282)	(35,810)
Asia-Pacific	2,667	(6,682)	(77,215)	(6,490)
Total income (loss) from operations	$ 9,575	$ (33,513)	$ (223,076)	$ (75,790)
Capital Expenditures				
United States and Other	$ 575	$ 802	$ 2,011	$ 9,610
Canada	4,158	3,156	12,261	8,565
Europe	473	998	1,090	4,017
Asia-Pacific	2,600	7,369	8,564	20,330
Total	$ 7,806	$ 12,325	$ 23,926	$ 42,522

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

	September 30, 2006	December 31, 2005
Assets		
United States and Other		
United States	$ 83,862	$ 134,360
Other	4,766	7,226
Total United States and Other	88,628	141,586
Canada		
Canada	109,274	157,155
Total Canada	109,274	157,155
Europe		
United Kingdom	21,787	35,685
Germany	12,915	13,374
Netherlands	2,253	13,379
Other	47,550	57,019
Total Europe	84,505	119,457
Asia-Pacific		
Australia	111,455	200,148
Other	8,281	22,743
Total Asia-Pacific	119,736	222,891
Total	$ 402,143	$ 641,089

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

	Three months ended September 30,		Nine months ended September 30,	
	2006	2005	2006	2005
Voice	$ 174,252	$ 223,031	$ 552,445	$ 690,557
Data/Internet	42,219	42,570	127,027	129,713
VOIP	31,231	24,829	90,085	71,785
Total	$ 247,702	$ 290,430	$ 769,557	$ 892,055

10. DISCONTINUED OPERATIONS

In May 2006, the Company entered into a Share Purchase Agreement (SPA) with Videsh Sanchar Nigam Limited (VSNL), a leading international telecommunications company and member of the TATA Group, whereby VSNL purchased 100% of the stock of Direct Internet Limited (DIL), whose wholly-owned subsidiary, Primus Telecommunications India Limited (PTIL), was primarily engaged in providing fixed broadband wireless Internet services to enterprise and retail customers in India. The Company owned approximately 85% of the stock of DIL through an indirect wholly-owned subsidiary. The remaining approximately 15% of the stock of DIL was owned by the manager of DIL and

PTIL, who had founded the predecessor companies. The total purchase consideration was $17.5 million. The Company received $13.0 million in net cash proceeds from the transaction at closing on June 23, 2006, after closing adjustments. Under the SPA, the Company agreed to certain non-compete provisions regarding the business of DIL and PTIL and is a party to the SPA for the purpose of guaranteeing indemnity obligations of its subsidiary selling the stock of DIL. The net assets of DIL were $8.9 million at June 23, 2006.

As a result of the sale, the Company s consolidated financial statements reflect India operations as discontinued operations for the nine months ended September 30, 2006 and the three and nine months ended September 30, 2005. Accordingly, revenue, costs, and expenses of the discontinued operations have been excluded from the respective captions in the consolidated statements of operations. The net operating results of the discontinued operations have been reported, net of applicable income taxes as income from discontinued operations.

Summarized operating results of the discontinued India operations for the nine months ended September 30, 2006 and the three and nine months ended September 30, 2005 are as follows (in thousands):

	Three Months Ended September 30,	Nine Months Ended September 30,	
	2005	2006	2005
Net revenues	$ 2,720	$ 5,653	$ 8,175
Operating expenses	2,098	4,476	6,333
Income from operations	622	1,177	1,842
Interest expense		(5)	(3)
Interest income and other income (expense)	58	45	29
Income (loss) before income tax	680	1,217	1,868
Income tax expenses	(78)	(78)	(153)
Income from discontinued operations	$ 602	$ 1,139	$ 1,715

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

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

Diluted income per common share adjusts basic income per common share for the effects of potentially dilutive common share equivalents. Potentially dilutive common shares primarily include the dilutive effects of common shares issuable under the Company s stock option compensation plans computed using the treasury stock method and the dilutive effects of shares issuable upon conversion of its 2003 Convertible Senior Notes, 2000 Convertible Subordinated Debentures, the Step Up Convertible Subordinated Debentures, and 5% Exchangeable Senior Notes.

For the three and nine months ended September 30, 2006, the following could potentially dilute income per common share in the future but were excluded from the calculation of diluted income (loss) per common share due to their antidilutive effects:

8.3 million shares issuable under the Company s stock option compensation plans,

-0- and 46.9 million shares, respectively, issuable upon the conversion of the 5% Exchangeable Senior Notes,

23.2 million shares issuable upon the conversion of the Step Up Convertible Subordinated Debentures,

8.3 million shares issuable upon conversion of the 2003 Convertible Senior Notes, and

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

For the three and nine months ended September 30, 2005, the following could potentially dilute income per common share in the future but were excluded from the calculation of diluted loss per common share due to their antidilutive effects:

8.1 million shares issuable under the Company s stock option compensation plans, 14.2 million shares issuable upon conversion of the 2003 Convertible Senior Notes, and

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

12. GUARANTOR/NON-GUARANTOR CONDENSED CONSOLIDATED FINANCIAL INFORMATION

PTHI s 2004 Senior Notes and 5% Exchangeable Senior Notes are fully and unconditionally and jointly and severally guaranteed by Primus Telecommunications Group, Incorporated (PTGI). Accordingly, the following consolidating condensed financial information as of September 30, 2006 and December 31, 2005, and for the three-month and nine-month periods ended September 30, 2006 and September 30, 2005 are included for (a) PTGI on a stand-alone basis; (b) PTHI and its subsidiaries; and (c) PTGI on a consolidated basis.

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

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS

(in thousands)

	For the Three Months Ended September 30, 2006			
	PTGI	**PTHI**	**Eliminations**	**Consolidated**
NET REVENUE	$	$ 247,702	$	$ 247,702
OPERATING EXPENSES				
Cost of revenue (exclusive of depreciation included below)		158,845		158,845
Selling, general and administrative	1,833	70,651		72,484
Depreciation and amortization		7,003		7,003
Gain (loss) on sale or disposal of assets		(205)		(205)
Total operating expenses	1,833	236,294		238,127
INCOME (LOSS) FROM OPERATIONS	(1,833)	11,408		9,575
INTEREST EXPENSE	(4,066)	(9,133)		(13,199)
ACCRETION ON DEBT DISCOUNT	222			222
INTEREST AND OTHER INCOME	40	805		845
FOREIGN CURRENCY TRANSACTION GAIN	1,605	2,291		3,896
INTERCOMPANY INTEREST	1,002	(1,002)		
EQUITY IN NET INCOME OF SUBSIDIARIES	3,252		(3,252)	
INCOME BEFORE INCOME TAXES	222	4,369	(3,252)	1,339
INCOME TAX EXPENSE	(101)	(1,117)		(1,218)
NET INCOME	$ 121	$ 3,252	$ (3,252)	$ 121

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS

(in thousands)

	For the Three Months Ended September 30, 2005			
	PTGI	**PTHI**	**Eliminations**	**Consolidated**
NET REVENUE	$	$ 290,430	$	$ 290,430
OPERATING EXPENSES				
Cost of revenue (exclusive of depreciation included below)		196,488		196,488
Selling, general and administrative	1,208	91,609		92,817
Depreciation and amortization		21,866		21,866
Loss on sale or disposal of assets		12,772		12,772
Total operating expenses	1,208	322,735		323,943
LOSS FROM OPERATIONS	(1,208)	(32,305)		(33,513)
INTEREST EXPENSE	(4,933)	(8,618)		(13,551)
LOSS ON EARLY EXTINGUISHMENT OF DEBT	(4,160)			(4,160)
INTEREST AND OTHER INCOME	44	736		780
FOREIGN CURRENCY TRANSACTION GAIN (LOSS)	(58)	2,032		1,974
INTERCOMPANY INTEREST	10,720	(10,720)		
EQUITY IN NET LOSS OF SUBSIDIARIES	(50,582)		50,582	
LOSS BEFORE INCOME TAXES	(50,177)	(48,875)	50,582	(48,470)
INCOME TAX EXPENSE	(1,072)	(1,707)		(2,779)
LOSS FROM CONTINUING OPERATIONS	(51,249)	(50,582)	50,582	(51,249)
INCOME FROM DISCONTINUED INDIA OPERATIONS, net of tax		602		602
NET LOSS	$ (51,249)	$ (49,980)	$ 50,582	$ (50,647)

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS

(in thousands)

	For the Nine Months Ended September 30, 2006			
	PTGI	**PTHI**	**Eliminations**	**Consolidated**
NET REVENUE	$	$ 769,557	$	$ 769,557
OPERATING EXPENSES				
Cost of revenue (exclusive of depreciation included below)		506,502		506,502
Selling, general and administrative	5,260	216,195		221,455
Depreciation and amortization		41,126		41,126
Loss on sale or disposal of assets		14,302		14,302
Asset impairment write-down		209,248		209,248
Total operating expenses	5,260	987,373		992,633
LOSS FROM OPERATIONS	(5,260)	(217,816)		(223,076)
INTEREST EXPENSE	(13,205)	(27,476)		(40,681)
ACCRETION ON DEBT DISCOUNT	(1,344)			(1,344)
CHANGE IN FAIR VALUE OF DERIVATIVES EMBEDDED WITHIN CONVERTIBLE DEBT	5,373			5,373
GAIN (LOSS) ON EARLY EXTINGUISHMENT OR RESTRUCTURING OF DEBT	10,374	(2,965)		7,409
INTEREST AND OTHER INCOME	104	3,306		3,410
FOREIGN CURRENCY TRANSACTION GAIN	4,128	4,392		8,520
INTERCOMPANY INTEREST	3,091	(3,091)		
EQUITY IN NET LOSS OF SUBSIDIARIES	(238,483)		238,483	
LOSS BEFORE INCOME TAXES	(235,222)	(243,650)	238,483	(240,389)
INCOME TAX EXPENSE	(309)	(3,387)		(3,696)
LOSS FROM CONTINUING OPERATIONS	(235,531)	(247,037)	238,483	(244,085)
INCOME FROM DISCONTINUED INDIA OPERATIONS, net of tax		1,139		1,139
INCOME FROM SALE OF DISCONTINUED INDIA OPERATIONS, net of tax		7,415		7,415
NET LOSS	$ (235,531)	$ (238,483)	$ 238,483	$ (235,531)

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

CONSOLIDATING CONDENSED STATEMENT OF OPERATIONS

(in thousands)

	For the Nine Months Ended September 30, 2005			
	PTGI	**PTHI**	**Eliminations**	**Consolidated**
NET REVENUE	$	$ 892,055	$	$ 892,055
OPERATING EXPENSES				
Cost of revenue (exclusive of depreciation included below)		592,599		592,599
Selling, general and administrative	4,642	291,253		295,895
Depreciation and amortization		66,001		66,001
Loss on sale of assets				
Loss on disposal of assets		13,350		13,350
Total operating expenses	4,642	963,203		967,845
LOSS FROM OPERATIONS	(4,642)	(71,148)		(75,790)
INTEREST EXPENSE	(15,221)	(24,351)		(39,572)
LOSS ON EARLY EXTINGUISHMENT OF DEBT	(5,865)			(5,865)
EQUITY INVESTMENT LOSS		(249)		(249)
INTEREST AND OTHER INCOME	114	2,247		2,361
FOREIGN CURRENCY TRANSACTION LOSS	(183)	(4,196)		(4,379)
INTERCOMPANY INTEREST	31,917	(31,917)		
EQUITY IN NET LOSS OF SUBSIDIARIES	(132,400)		132,400	
LOSS BEFORE INCOME TAXES	(126,280)	(129,614)	132,400	(123,494)
INCOME TAX EXPENSE	(3,183)	(4,501)		(7,684)
LOSS FROM CONTINUING OPERATIONS	(129,463)	(134,115)	132,400	(131,178)
INCOME FROM DISCONTINUED INDIA OPERATIONS, net of tax		1,715		1,715
NET LOSS	$ (129,463)	$ (132,400)	$ 132,400	$ (129,463)

PRIMUS TELECOMMUNICATIONS GROUP, INCORPORATED

CONSOLIDATING CONDENSED BALANCE SHEET

(in thousands)

	September 30, 2006			
	PTGI	PTHI	Eliminations	Consolidated
ASSETS				
CURRENT ASSETS:				
Cash and cash equivalents	$ 5,563	$ 65,265	$	$ 70,828
Accounts receivable		119,419		119,419
Prepaid expenses and other current assets	514	25,387		25,901
Total current assets	6,077	210,071		216,148
INTERCOMPANY RECEIVABLES		244,389	(244,389)	
INVESTMENTS IN SUBSIDIARIES	43,957		(43,957)	
RESTRICTED CASH		9,313		9,313
PROPERTY AND EQUIPMENT Net		108,539		108,539
GOODWILL		35,183		35,183
OTHER INTANGIBLE ASSETS Net		3,099		3,099
OTHER ASSETS	3,991	25,870		29,861
TOTAL ASSETS	$ 54,025	$ 636,464	$ (288,346)	$ 402,143
LIABILITIES AND STOCKHOLDERS DEFICIT				
CURRENT LIABILITIES:				
Accounts payable	$ 553	$ 75,003	$	$ 75,556
Accrued interconne				